CIVIL RIGHTS

and the

Mortgage Crisis

UNITED STATES COMMISSION ON CIVIL RIGHTS

September 2009

U.S. COMMISSION ON CIVIL RIGHTS

The U.S. Commission on Civil Rights is an independent, bipartisan agency established by Congress in 1957. It is directed to:

- Investigate complaints alleging that citizens are being deprived of their right to vote by reason of their race, color, religion, sex, age, disability, or national origin, or by reason of fraudulent practices.
- Study and collect information relating to discrimination or a denial of equal protection of the laws under the Constitution because of race, color, religion, sex, age, disability, or national origin, or in the administration of justice.
- Appraise federal laws and policies with respect to discrimination or denial of equal protection of the laws because of race, color, religion, sex, age, disability, or national origin, or in the administration of justice.
- Serve as a national clearinghouse for information in respect to discrimination or denial of equal protection of the laws because of race, color, religion, sex, age, disability, or national origin.
- Submit reports, findings, and recommendations to the President and Congress.
- Issue public service announcements to discourage discrimination or denial of equal protection of the laws.

MEMBERS OF THE COMMISSION

U.S. Commission on Civil Rights
624 Ninth Street, NW
Washington, DC 20425

(202) 376-8128 voice
(202) 376-8116 TTY

www.usccr.gov

This report is available on disk in ASCII Text and Microsoft Word 2003 for persons with visual impairments. Please call (202) 376-8110.

Cover photo: “Suburban American Flag.” David Gilder, 2006. Photo: istockphoto.com.

CIVIL RIGHTS

and the

Mortgage Crisis

UNITED STATES COMMISSION ON CIVIL RIGHTS

September 2009

LETTER OF TRANSMITTAL

The President
The President of the Senate
The Speaker of the House

Sirs and Madam:

The United States Commission on Civil Rights transmits this report, *An Examination of Civil Rights Issues With Respect to the Mortgage Crisis,* pursuant to Public Law 103-419. The purpose of the report is to examine whether federal efforts to increase homeownership rates among minority and low-income individuals may have unintentionally weakened underwriting standards and lending policies to the point that too many borrowers were vulnerable to financial distress and heightened risk of default, thereby setting conditions for the current mortgage crisis. It also examines the policies of federal agencies in enforcing prohibitions against mortgage fraud and lending discrimination.

To that end, the Commission studied federal policies aimed at increasing low-income and minority homeownership, including the Community Reinvestment Act and the Department of Housing and Urban Development's lending goals for government-sponsored enterprises (GSEs) Fannie Mae and Freddie Mac, and the critiques regarding the relationship of such policies to the mortgage crisis. As part of its analysis, the Commission also considered the impact of the growth of securitization on lending practices, including the availability of subprime mortgages and other kinds of credit, as well as the manner in which such credit was made available on the secondary market. This analysis involved gathering information from the GSEs and some eleven federal agencies with various levels of regulatory responsibility over the housing market and lending standards.

The Commission also looked at issues of predatory lending, mortgage fraud, and lending discrimination and assessed the efforts of eight federal agencies with responsibility for enforcing the Fair Housing and Equal Credit Opportunity Acts to combat such practices. The result, we hope, will contribute to the growing body of literature for consideration by policy makers as they examine whether existing lending policies require revision, modification, or elimination to avoid a future similar crisis while enhancing the possibility that the American dream of homeownership remains an attainable goal for low and middle-income Americans.

On August 7, 2009, the Commission approved this report. The vote was as follows: Chapters 1-5 and the appendix were approved by Commissioners Reynolds, Thernstrom, Kirsanow and Taylor, with Commissioners Yaki, Melendez, Heriot and Gaziano abstaining. The Commission declined to adopt findings and recommendations to this report with six Commissioners voting against adoption, and with Vice Chair Thernstrom and Commissioner Melendez abstaining. The report includes a joint statement and separate rebuttal statements submitted by Commissioners Melendez and Yaki, a separate statement by Vice Chair Thernstrom, and a joint rebuttal statement by Commissioners Gaziano, Reynolds, Kirsanow, and Taylor.

For the Commissioners,

Gerald A. Reynolds
Chairman

TABLE OF CONTENTS

FIGURES

TABLES

INTRODUCTION AND OVERVIEW

INTRODUCTION AND OVERVIEW

Overview

Over the last several decades, the federal government has adopted a series of policies to address the persistent gap in homeownership rates between whites and racial and ethnic minorities. These efforts, undertaken by administrations of both major political parties, sought to increase minority homeownership through a variety of means. The initial steps focused on the adoption of laws prohibiting discrimination based on characteristics such as race, sex, religion, etc. More recently, federal laws and policies have sought to affirmatively further homeownership for those of low- and moderate-income.

The most important of these policies involve the implementation of the Community Reinvestment Act and the Department of Housing and Urban Development's (HUD) lending goals for government-sponsored enterprises such as the Federal National Mortgage Association (Fannie Mae) and the Federal Home Loan Mortgage Corporation (Freddie Mac). There is little doubt that, over the last 15 years, homeownership generally, and minority homeownership in particular, has increased. For example, from 1994 to 2004, overall U.S. homeownership increased from 64 percent to 69 percent—an increase of 5 percentage points in just over a decade. The increase in minority homeownership has been even more substantial. During the same time period, Hispanic homeownership rates increased 6.9 percentage points while Black homeownership rates increased 6.8 percentage points.

Moreover, although the mortgage crisis may not have run its course, figures from 1994 through 2008 indicate that overall homeownership rates demonstrate a net gain despite the advent of the crisis and increased rates of foreclosures. Specifically, overall homeownership from 1994 to 2008 increased by 3.8 percentage points, White homeownership by 4.0 percentage points, Black homeownership by 5.1 percentage points, Hispanic homeownership by 7.9 percentage points, Asian/Native Hawaiian homeownership by 8.2 percentage points, and American Indian homeownership by 4.8 percentage points.

The current mortgage crisis, however, raises questions as to whether the policies that helped increase homeownership may have come with a hidden cost. Specifically, questions have been raised as to whether the actions taken to affirmatively further homeownership might have, unintentionally, weakened underwriting standards and lending policies to the point that too many borrowers were vulnerable to financial distress and a heightened risk of default.

This report examines civil rights issues with respect to the mortgage crisis so that policy makers can determine whether existing policies should be revised, modified, or ended. We believe that this focused contribution will help determine the effectiveness of the various federal laws and policies adopted to increase homeownership for minorities and low- and moderate-income individuals.[1]

---

[1] The U.S. Commission on Civil Rights has historically reviewed housing policy and antidiscrimination laws. *See, e.g.,* U.S. Commission on Civil Rights, *USCCR Statutory Reports 1961*, 1961; U.S. Commission on Civil Rights, *Federal Installations and Equal Housing Opportunity*, March 1970; U.S. Commission on Civil Rights, *Home Ownership For Lower Income Families: A Report on the Racial and Ethnic Impact of the Section 235 Program*, June 1971; U.S. Commission on Civil

Scope and Methodology[2]

This study is presented in three parts. Part I is an overview of federal policies adopted to increase minority homeownership, critiques regarding the relationship of such policies to the mortgage crisis, and an analysis of the effects of the federal policies to increase minority homeownership.

In preparing this section, the Commission sought and analyzed information of regulatory enforcement activities from 11 federal agencies and government-sponsored enterprises. In addition, it assembled historic trend data on homeownership disparities and mortgage lending statistics from the Census Bureau and the Board of Governors of the Federal Reserve System (the Federal Reserve), which regulates collection of a statutorily-mandated database on loans under the Home Mortgage Disclosure Act. The Commission also obtained data from Fannie Mae and Freddie Mac with regard to such matters as mortgages issued, overall financial performance, and lending standards. The effort included an internet document search and literature review as well as contacts with researchers and financial analysts who study relevant issues.

Part II of the report addresses the issue of predatory lending, mortgage fraud, and mortgage lending discrimination. The section examines the roles and policies of various federal agencies in enforcing prohibitions against mortgage fraud and lending discrimination. For this purpose, the Commission studied the eight agencies assigned the responsibility of enforcing the Fair Housing Act and the Equal Credit Opportunity Act. These agencies are HUD, the Department of Justice, the Federal Trade Commission, and the five agencies which comprise the Federal Financial Institutions Examination Council – the Federal Reserve, the National Credit Union Administration, the Federal Deposit Insurance Corporation, the Office of Thrift Supervision, and the Office of the Comptroller of the Currency.

Rights, *Mortgage Money: Who Gets It?: A Case Study in Mortgage Lending Discrimination in Hartford, Connecticut*, June 1974; U.S. Commission on Civil Rights, *The Federal Fair Housing Enforcement Effort*, March 1979; U.S. Commission on Civil Rights, *Housing: Chicago Style, A Consultation*, October 1982; U.S. Commission on Civil Rights, *A Sheltered Crisis: The State of Fair Housing in the Eighties*, September 1983; U.S. Commission on Civil Rights, *Issues in Housing Discrimination, Vol. I (Papers Presented) & II (Proceedings)*, November 1985; U.S. Commission on Civil Rights, *Prospects and Impacts of Losing State and Local Agencies from the Federal Fair Housing System*, September 1992; U.S. Commission on Civil Rights, *The Fair Housing Amendments Act of 1988: The Enforcement Report*, September 1994; U.S. Commission on Civil Rights, *Ten-Year Check-Up: Have Federal Agencies Responded to Civil Rights Recommendations? Vol. IV*, September 2004.

[2] For a more detailed explanation of the methodology used by the Commission in preparing this report, please see the last section of the report entitled "Methodology Used in Report."

Finally, Part III of the study examines the role of credit scoring and other factors used by lenders in the granting and pricing of loans. This section analyzes whether such tools are objective predictors of creditworthiness.

In preparing this report, the Commission was aided by the written statements and oral testimony of those appearing at the briefing held on this topic on March 20, 2009.[3]

---

[3] The written statements and oral testimony relating to the March 20, 2009 briefing are available at www.usccr.gov. The panelists were: David Berenbaum, National Community Reinvestment Coalition; Brian Brooks, O'Melveny & Myers, LLP; Luke Brown, Federal Deposit Insurance Corporation; Glenn Canner, Board of Governors of the Federal Reserve System; Jim Carr, National Community Reinvestment Coalition; Leonard Chanin, Board of Governors of the Federal Reserve System; Marsha Courchane, Charles River Associates; Eileen Harrington, Federal Trade Commission; Howard Husock, Manhattan Institute; Stan Liebowitz, University of Texas-Dallas; Ken Markison, Mortgage Bankers Association; Alfred Pollard, Federal Housing Finance Agency; Lisa Rice, National Fair Housing Alliance; John Weicher, Center for Housing and Financial Markets; and Barry Wides, Office of the Comptroller of the Currency.

PART I: MINORITY HOMEOWNERSHIP

CHAPTER 1: OVERVIEW OF FEDERAL POLICIES TO INCREASE MINORITY HOMEOWNERSHIP AND CRITIQUES REGARDING THEIR RELATIONSHIP TO THE MORTGAGE CRISIS

There are two primary federal programs meant to increase homeownership in minority and other underserved communities:[1] the Community Reinvestment Act (CRA) and the affordable housing goals established by the U.S. Department of Housing and Urban Development (HUD) for government-sponsored enterprises (GSEs) such as the Federal National Mortgage Association (Fannie Mae) and the Federal Home Loan Mortgage Corporation (Freddie Mac).

In both cases, the federal policies in question do not provide for direct federal subsidies or transfer payments. Instead, the policies seek to increase homeownership through an indirect process, requiring private entities to comply with goals and performance criteria.

The adoption and subsequent modifications of the HUD lending goals and the CRA have been the subject of extensive debate and challenges. This section will describe the stated goals behind these policies and discuss some of the issues that have been raised about the role these policies may have had with regard to the mortgage crisis.

I. Bipartisan Effort

The effort to increase homeownership generally, and minority homeownership in particular,[2] has been bipartisan in nature. In recent decades, both political parties have sought to increase the rate of homeownership and to narrow the gap between Whites and minorities in this area.[3]

---

[1] While both policies do not explicitly indicate they are addressing minority homeownership, public statements by both the Clinton and Bush administrations made clear that increasing minority homeownership was a major goal of both policies. *See also* U.S. Department of the Treasury, *The Community Reinvestment Act After Financial Modernization: A Baseline Report*, April 2000, p. ES-8 ("Although the CRA does not focus on race, the statute had its origins in concerns about redlining, and evidence of discrimination adversely affects the regulators' evaluation of a depository institution's CRA performance."); John Weicher, Written Statement to the U.S. Commission on Civil Rights, March 20, 2009, p. 3 (hereafter referred to as Weicher, Statement) ("The affordable housing goals are not set in terms of the race or ethnicity of the borrower … There is, however, policy interest in the extent to which borrowers …are members of minority groups.").

[2] *See* U.S. Department of the Treasury, *The Community Reinvestment Act After Financial Modernization: A Baseline Report* at p. ES-8. ("Although the CRA does not focus on race, the statute had its origins in concerns about redlining, and evidence of discrimination adversely affects the regulators' evaluation of a depository institution's CRA performance.") *See also* Weicher, Statement at p. 3. ("The affordable housing goals are not set in terms of the race or ethnicity of the borrower … There is, however, policy interest in the extent to which borrowers …are members of minority groups.").

[3] The push to increase homeownership of low-income individuals was also backed by community groups such as the National People's Action on Housing, which brought pressure on the government, as well as Fannie Mae and Freddie Mac, to loosen credit standards. In describing the efforts of one such group, one author noted:

> [The National People's Action on Housing organization] would figure out how the entire American mortgage system functioned, take it apart, and put it back together again as a machine for fixing broken neighborhoods. Bolstered by the Community Reinvestment Act, they would use community organizing to take on every force that stood between

Many of the significant changes to both the CRA and the HUD lending goals began under President Clinton.

Under President Clinton's direction, HUD

> work[ed] with dozens of national leaders in government and the housing industry to implement the National Homeownership Strategy, an unprecedented public-private partnership to increase homeownership to a record-high level over the next 6 years.[4]

As President Clinton explained:

> Since 1993, nearly 2.8 million new households have joined the ranks of America's homeowners, nearly twice as many as in the previous two years. But we have to do a lot better. The goal of this strategy, to boost homeownership to 67.5 percent by the year 2000, would take us to an all-time high, helping as many as 8 million American families across that threshold.[5]

The Clinton administration's goals were summarized in the policy document, *The National Homeownership Strategy: Partners in the American Dream*, issued by HUD in May 1995. This report made clear that it was federal policy to attempt to close the homeownership gap between Whites and minorities.[6]

> Chicago residents and access to home loans. It would be a kind of democratic coup, where the nation's financial powers would have to respond to the popular will.
>
> * * *
>
> To do that, … Fannie Mae would have to do business very differently, and a little more recklessly. It would have to tolerate late mortgage payments, at least sometimes. It had to accept that old buildings in cities had some value, no matter what the appraisal manual said. The company would have to lower its minimum required down payment, from 10 to 5 or even 3 percent. And it would have to allow borrowers to take on more debt, compared to their income, than anyone had previously considered reasonable.

ALYSSA KATZ, OUR LOT: HOW REAL ESTATE CAME TO OWN US pp. 14, 24 (2009).

4 U.S. Department of Housing and Urban Development, Urban Policy Brief, Number 2, August 1995, <http://www.huduser.org/publications/txt/hdbrf2.txt> (last accessed July 13, 2009). *See also* U.S. Department of Housing and Urban Development, *The National Homeownership Strategy: Partners in the American Dream*, May 1995 (hereafter cited as HUD, *National Homeownership Strategy*).

5 President William J. Clinton, Remarks on the National Homeownership Strategy (June 5, 1995), http://www.presidency.ucsb.edu/ws/index.php?pid=51448> (last accessed July 13, 2009).

6 *See* KATZ at p. 34:

> "We really did believe that assets and wealth-building changed the way that people thought about the future, their planning horizons, their way of building wealth," says Michael Stegman, who headed policy development for Clinton's HUD and recommended the National Homeownership Strategy's goals …. Year by year, payment by payment, the new homeowners would move into what President Clinton liked to call the "economic mainstream." Rather than government spending its money on aid to families month after month, it would reward them for the desired behavior of saving for the future.

> Across all income levels, African-American and Hispanic-American households have lower homeownership rates compared to other groups with comparable incomes. At the same time, low- and moderate-income households are much less likely than higher-income households to own homes. Breaking down racial and ethnic barriers and increasing access for other underserved households will extend homeownership opportunities to millions of families and enable minority households to own homes in a much wider range of communities.[7]

The report further noted that the federal government had:

> a special responsibility and an important opportunity to target underserved populations and communities, including low- and moderate-income households, minorities, young adults, families with children, legal immigrants, people with disabilities, Native Americans, and residents of inner-city neighborhoods and rural areas.[8]

To meet these goals, the report sought federal policies that would increase down payment assistance, encourage lenders to expand creative financing[9] and adopt more flexible mortgage underwriting criteria.[10]

The drive to increase homeownership was pressed with equal force by the Bush administration. In hosting a conference on minority homeownership in October 2002, President Bush stated that: "we want everybody in America to own their home" and that we should be "a nation of homeowners."[11] The President also expressed concern for disparities in homeownership, saying,

> Two-thirds of all Americans own their homes, yet we have a problem here in America because few[er] than half of the Hispanics and half the African Americans own the[ir] home[s]. That's a homeownership gap … it's a gap that we've got to work together to

---

[7] HUD, *National Homeownership Strategy* at p. 1-4. *See also* KATZ at pp. 27–37.

[8] HUD, *National Homeownership Strategy* at p. 1-7. *See also id*. at pp. 1-4, 6-7.

[9] *See id.* at p. 1–3. *See also* Binyamin Appelbaum, Carol D. Leonnig and David S. Hilzenrath, *How Washington Failed to Rein in Fannie, Freddie*, WASH. POST, Sept. 14, 2008 ("The Clinton administration wanted to expand the share of Americans who owned homes, which had stagnated below 65 percent throughout the 1980s.").

[10] *See* HUD, *National Homeownership Strategy* at p. 4-1 ("It is vital that this change in the mortgage finance system be guided by a commitment to increase opportunities for homeownership for more families, particularly for low- and moderate-income and minority families, and to increase the national homeownership rate to an all-time high …Financing strategies, fueled by the creativity and resources of the private and public sectors, should address … these financial barriers to homeownership."). *See also id.* at pp. 3-1, 4-13, 6-7; HUD, *Urban Policy Brief*, No. 2 (August 1995) (This publication urged lenders to make financing more available, affordable and flexible by taking such steps as reducing down payment requirements and by increasing the availability of alternative financing products.); KATZ at p. 35 ("Clinton's Department of Housing and Urban Development pushed lenders to sign agreements committing them to adopt more flexible loan policies and market their products to new groups of consumers.").

[11] President George W. Bush, Remarks at the White House Conference on Minority Homeownership (October 15, 2002), <http://www.gpo.gov/fdsys/pkg/WCPD-2002-10-21/pdf/WCPD-2002-10-21-Pg1772.pdf> (last accessed July 13, 2009).

> close for the good of our country, for the sake of a more hopeful future. We've got to knock down the barriers that have created a homeownership gap.[12]

The policies President Bush adopted to help close this gap included (i) the establishment of an "American Dream Down Payment Fund" to provide grants to local governments to help first-time home owners; (ii) providing a single-family housing credit to encourage the construction of single-family homes in neighborhoods where affordable housing is scarce; and (iii) providing funding to conduct homebuyer education.[13]

The President's remarks at the housing conference echoed goals he had set forth several months earlier:

> I've set this goal for the country. We want 5.5 million more homeowners by 2010 – [a] million more minority homeowners by 2010. Five-and-a-half million families by 2010 will own a home. That is our goal. It is a realistic goal. But it's going to mean we're going to have to work hard to achieve the goal, all of us. And by all of us, I mean not only the federal government, but the private sector, as well.[14]

In 2006, President Bush praised the House of Representatives' passage of the "Expanding American Homeownership Act," noting that "[b]y providing the FHA with increased flexibility for mortgage down payment requirements and the authority to tailor financing to suit a family's unique situation, this bill will improve FHA's ability to help lower and moderate-income families in achieving the American Dream."[15]

Reflecting the drive to increase homeownership rates, both administrations increased the HUD lending goals, with the low- and moderate-income goal rising from 40 percent in 1996 to 55 percent in 2007.[16] Fannie Mae and Freddie Mac were expected to perform at levels more reflective of their unique position in the mortgage lending market. In April 2005 testimony before the House Committee on Financial Services, President Bush's HUD Secretary, Alphonso Jackson, stated:

> To better ensure these two GSEs' leadership in the mortgage market, HUD will require that the GSEs at least 'meet the market' – in other words, their purchases of mortgages in each goal category must be proportional to the share of all mortgages in the conventional conforming market that fall within that category. In the past, HUD's goals have been set 'below the market.' Other conventional lenders – without the GSEs' Charter Act

---

[12] *Id.*

[13] Press Release, White House, Office of the Press Secretary, President Hosts Conference on Minority Home Ownership (October 15, 2002).

[14] President George W. Bush, Remarks by the President on Home Ownership (June 18, 2002), <http://georgewbush-whitehouse.archives.gov/news/releases/2002/06/print/20020618-1.html> (last accessed July 13, 2009). The President proclaimed June 2002 "National Homeownership Month." President George W. Bush, Proclamation, *National Home Ownership Month, 2002* (June 4, 2002).

[15] Press Release, White House, Office of the Press Secretary, President Pleased by House Passage of the "Expanding American Homeownership Act of 2006" (July 26, 2006), <http://georgewbush-whitehouse.archives.gov/news/releases/2006/07/20060726.html> (last accessed July 13, 2009).

[16] *See* Table 1.1, *infra*.

> privileges – have served lower-income families and underserved areas better than the two GSEs have done. HUD believes the GSEs can do at least as well as other conventional lenders.[17]

In order to analyze the effects of these two policies, it is first necessary to examine their evolution over the last several decades. The following section examines both the CRA and the HUD lending goals as they have evolved.

II. The Community Reinvestment Act

The CRA[18] was enacted in 1977 to encourage depository institutions to more effectively meet the credit needs of their communities.[19] To that end, the statute requires periodic evaluation of each insured depository institution's record in helping meet the credit needs of its entire community, consistent with safe and sound lending practices. CRA applies to federally-insured banks, state banks, and federally and state-chartered thrifts.

A. Evolution of the CRA

1989 Amendments

The nature and execution of CRA examinations began to change significantly in 1989. "Banking regulators formulated a new CRA policy statement stating that lenders would be evaluated on the basis of their actual performance record at the time of examination, and not merely on promises for improvements or their existing record in reaching out to the community."[20]

---

[17] Testimony before the U.S. House of Representatives Committee on Financial Services, 109th Cong. (Apr. 13, 2005) (Statement of Alphonso Jackson, Secretary, U.S. Department of Housing and Urban Development), <http://www.hud.gov/offices/cir/test041305.cfm> (last accessed July 13, 2009). *See* Weicher, Statement at p. 3. (The terms "lead the market" and "lag the market" have been described as follows: "This is shorthand for whether the loans in a given goal category are included in GSE purchases to the same extent that they are in the conventional conforming market. To give a numerical example, if loans to borrowers with incomes below the local median represent 50% of all loans in the conventional conforming market in a particular year, then the GSEs are 'leading the market' if such loans represent 51% or more of their purchases, and they are 'lagging the market' if such loans represent 49% or less of their purchases. Under the targets established as of 1996 and 2000, the GSEs were not asked to 'lead the market' in any goal category; the targets were set so that they could be fulfilled even though the GSEs 'lagged the market.' Under the targets set as of 2005, the GSEs were asked to 'meet the market.' To avoid creating problems for the GSEs, the targets were phased in year-by-year over the next four years.").

[18] Community Reinvestment Act, Pub. L. No. 95-128, Title VIII, § 802.91 Stat. 1147 (1977) (codified as amended at 12 U.S.C. §§ 2901–2908 (2006)).

[19] 123 Cong. Rec. 1958 (1977).

[20] U.S. Department of the Treasury, *The Community Reinvestment Act After Financial Modernization: A Baseline Report* at pp. 7–8. Also in 1989 the Federal Reserve denied a merger application on CRA grounds for the first time, "ruling that commitments and plans to improve CRA performance by Continental Bank could not serve as a substitute for the established record of CRA performance required by the statute." *Id.*

Also in 1989, Congress, through the Financial Institutions Reform, Recovery, and Enforcement Act (FIRREA),[21] required regulators to publicly disclose an institution's CRA rating as well as a written performance evaluation.[22] The 1989 amendments also created a four-tiered descriptive rating system describing the lenders' record of meeting community credit needs: (i) outstanding, (ii) satisfactory, (iii) needs to improve, and (iv) substantial noncompliance. Replacing the prior numeric scale, the amendments also required banking regulators to prepare a public, written evaluation of the institution's CRA examination record.[23]

1995 Regulatory Amendments

In 1995, federal regulators further refined CRA evaluation standards by revising their CRA regulations.[24] "Responding to widespread complaints from both industry and advocacy groups that, despite the 1989 revisions, CRA evaluations still relied too heavily on the processes by which depository institutions attempted to meet their CRA obligations, the 1995 revisions focused explicitly on an institution's actual performance."[25]

The 1995 regulations established separate compliance tests for four categories of depository institutions: large, small, wholesale, and limited-purpose institutions.[26] For institutions classified as "large retail," examination ratings are based on the sum of scores relating to the institution's lending, investment, and financial services provided to their entire communities with lending weighted more heavily. Small banks and thrifts are evaluated "under a streamlined approach that focuses on lending-related criteria."

---

[21] Financial Institutions Reform, Recovery, and Enforcement Act, Pub. L. No. 101-73, 103 Stat. 183 (1989).

[22] 12 U.S.C. § 2906. (Prior to 1989, ratings of a financial institution's CRA record were confidential.)

[23] *Id*.

[24] Community Reinvestment Act Regulations, 60 Fed. Reg. 22156-2226 (1995) (codified at 12 C.F.R. pts. 25, 228, 345, 563e, 203 (2006)).

[25] U.S. Department of the Treasury, *The Community Reinvestment Act After Financial Modernization: A Baseline Report* at p. 9.

[26] 60 Fed. Reg. 22156 (May 4, 1995). *See* Federal Financial Institutions Examination Council, *Explanation of the Community Reinvestment Act Asset Threshold Change and Federal Reserve* (2008), <http://www.ffiec.gov/cra/pdf> (last accessed July 15, 2009) (The 1995 CRA regulations defined small depository institutions as those with less than $250 million in assets that were either independent of a holding company or an affiliate of a holding company that had total bank and thrift assets of less than $1 billion. However, under the 2009 annual asset-size threshold adjustments, a small institution is one that, as of December 31 of either of the prior two calendar years, had assets of less than $1.109 billion, without regard to holding company affiliation.) *See also* Press Release, Board of Governors of the Federal Reserve, Federal Deposit Insurance Corporation, Office of the Comptroller of the Currency, and Office of Thrift Supervision, (Dec. 17, 2008), <http://www.federalreserve.gov/newsevents/press/bcreg/20081217a.html> (last accessed July 15, 2009). Agencies Release Annual CRA Asset-Size Threshold Adjustments for Small and Intermediate Small Institutions (The regulations also provided an alternative option for an institution to be examined under a "strategic plan" of measurable goals and objectives, with input from its community and approval from its federal banking regulator. Wholesale banks are not in the business of making home mortgages and are therefore not addressed in this report.). Limited purpose banks offer only a narrow product line of other than traditional retail lending products required to be evaluated under the lending test, including home mortgage loans, so they also should not be addressed.

Investments and service activities may be considered at the small institution's option in order to improve a rating from satisfactory to outstanding.[27]

The 1995 revisions include consideration of institutions' community development activities as part of large retail institution performance tests. Finally, the 1995 regulations require regulating agencies to publish a list of banks scheduled for CRA examinations in the upcoming quarter, a requirement conducive to public comment.

2005 Regulatory Amendments

In August 2005, OCC, the Federal Reserve, and the FDIC amended their CRA regulations. One key change was to redefine "small bank" to be those with assets of less than $1 billion, adjusted annually for inflation. Another key change was creating a new category of "intermediate small banks" for those with assets between $250 million and $1 billion. These changes were a response to claims by banks that the asset threshold to qualify as a small bank was too low.[28] OTS followed suit with respect to savings associations in March 2007.

As part of these amendments, the agencies were to make annual adjustments to the asset-size thresholds to define "small" and "intermediate small" banks and thrifts. For 2009, a "small institution" under the small bank lending test is defined as having assets under $277 million as of December 31 of either of the prior two calendar years. An "intermediate small institution" is defined as having assets from $277 million to just under $1.109 billion as of December 31 of the prior two years. "Large institutions" have total assets of at least $1.109 billion for December 31 of <u>both</u> of the prior two years.[29]

B. Agencies and Their Evaluation Authority

Four agencies have responsibility for evaluating the CRA performance of the institutions they supervise: OCC, the Federal Reserve, the FDIC, and OTS. This responsibility is assigned in accordance with each agency's oversight responsibility.[30]

---

[27] U.S. Department of the Treasury, *The Community Reinvestment Act After Financial Modernization* at p. 10.

[28] Josh Silver and Richard Marisco, *An Analysis of the Implementation and Impact of the 2004-2005 Amendments to the Community Reinvestment Act Regulations: The Continuing Importance of the CRA Examination Process*, 53 N.Y.L. SCH. L. REV. 271, 277 (2008/2009).

[29] 12 C.F.R. 345.12(u).

[30] The Board of Governors of the Federal Reserve System oversees bank holding companies, nonbank subsidiaries of bank holding companies, State-chartered banks that are members of the Federal Reserve System, and the U.S. operations of foreign banking organizations. It also regulates the foreign activities and investments of the Federal Reserve member banks, and Edge Act corporations.

The Office of the Comptroller of the Currency supervises national banks and federal branches and agencies of foreign banks.

The Federal Deposit Insurance Corporation oversees State-chartered banks and savings banks that are not members of the Federal Reserve System and foreign banks having insured branches.

The Office of Thrift Supervision oversees federal savings associations and also supervises State-chartered thrifts and thrift holding companies.

Each designated agency evaluates the extent to which lending entities help meet the credit needs of their entire communities, including low- and moderate-income neighborhoods, consistent with the safe and sound lending standards. The agencies consider this record in evaluating the applications of covered lending institutions for new branches and relocation of existing branches, as well as such activities as mergers, consolidations, and charter changes.[31]

Examinations

Each of the four banking regulators assesses CRA compliance via periodic examinations. CRA exams evaluate the extent to which banks respond to the needs of their local communities, and, based on the relevant agency's assessment of the bank's responsiveness to those needs, assigns a rating. Exams vary according to the asset size and type of bank undergoing examination.

The four agencies have developed identical examination procedures for the various types of institutions.[32] These extensive detailed procedures vary depending on the size and business strategy of

---

[31] 12 U.S.C. § 2903(a) (2008).

[32] By way of example, highlights of the 2007 examination procedures for small institutions are as follow:

Scope: For institutions with more than one assessment area, to determine which assessment areas to evaluate under a full scope review, consider, among other factors:

- the level of the institution's lending activity in the different assessment areas, including low- and moderate-income areas;
- the number of other institutions in the different assessment areas and the importance of the institution under examination in serving the different areas, particularly any areas with relatively few other providers of financial services;
- the existence of apparent anomalies in the reported HMDA data for any particular assessment area;
- the institution's prior CRA performance in different assessment areas; and
- comments from the public regarding the institution's CRA performance.

An assessment area is a geographic area delineated in accordance with each responsible agency's regulations.

Performance Context: A review of, among other things,

- relevant worksheets and other agency information to obtain relevant demographic, economic and loan data for each assessment area under review;
- relevant reports including Call Reports, Thrift Financial Reports, Uniform Bank Performance Reports, annual reports, supervisory reports; and prior CRA evaluations, as well as a review of prior CRA evaluations of institutions of similar size that serve the same or similar assessment areas;
- information the institution may provide on its local community and economy, its lending capacity, etc.; and
- the institution's public file for any comments received by the institution since the last CRA performance evaluation.

The examination procedures for small banks, cited below as an example since most institutions fall into this category, include an evaluation of the following:

Assessment Area: A review of the institution's assessment area for conformance with regulatory requirements.

Performance Criteria: Include,

A review of the assessment area, performance criteria including loan-to-deposit analysis:

- comparison of credit extended inside and outside of the assessment area(s);
- distribution of credit within the assessment area(s);
- review of complaints;
- investments and services (at the institution's option to enhance a "satisfactory" rating)

the institution being examined: (i) small, (ii) intermediate small, (iii) large, and (iv) with a community development test for institutions with a wholesale or limited purpose designation. All institutions have the option of being evaluated under a strategic plan.[33] Every institution is evaluated in light of its performance context, outlined below:

Examination Frequency

CRA provides that, with limited exceptions, “small banks” (or other regulated financial institutions) shall be subject to routine examination 1) not more than once every 60 months for an institution that has achieved a rating of “outstanding record of meeting community credit needs” at its most recent examination, 2) not more than once every 48 months for an institution that has received a rating of “satisfactory record of meeting community credit needs” at its most recent examination, and 3) as deemed necessary by the appropriate federal agency for an institution that has received a rating of less than “satisfactory record of meeting community credit needs” at its most recent examination.[34] Larger regulated financial institutions are subject to examination more frequently; for example, OTS examines large savings associations every 24 months.[35]

Ratings Generally

CRA ratings are available to the public, and each agency posts the evaluation results on its website. From the sample reviewed by the Commission, “satisfactory” is by far the most common rating. For example, the Federal Reserve posted 99 evaluations of small banks in 2008. Ninety-four of those small banks received “satisfactory” ratings, with the remaining five receiving “outstanding” ratings. In that same year, the Federal Reserve posted 59 intermediate small bank evaluations and 42 large bank evaluations, with 50 and 33 “satisfactory” ratings respectively. No small, intermediate small, or large banks received ratings below “satisfactory” for this period.[36]

Ratings: The examination procedures set forth an extensive and detailed set of instructions for determining an institution’s rating. [Ratings are maintained by the Federal Financial Institutions Examination Council and are available at http://www.ffiec.gov/craratings/default.aspx (last accessed July 15, 2009).]

Office of the Comptroller of the Currency, Federal Reserve Board, Federal Deposit Insurance Corporation, and Office of Thrift Supervision, *Small Institution CRA Examination Procedures* (July 2007). Available at <http://www.ffiec.gov/cra/pdf/cra_exsmall.pdf> (last accessed July 15, 2009).

As noted above, small banks are subject to streamlined examinations focusing on lending. Large banks are subject to more extensive examinations, with ratings based on the sum of scores relating to the institution’s lending, investment, and financial services provided to their entire communities with lending weighted more heavily.

[33] An institution may elect to be evaluated under the strategic plan option. A strategic plan sets forth goals for satisfactory (and, where appropriate, outstanding) performance, and must be approved by the relevant agency.

[34] 12 U.S.C. § 2908 (a) (2008).

[35] Office of Thrift Supervision, *CRA History and OTS’s CRA Responsibilities*, <http://www.ots/treas.gov/?p=CRAHistoryOTSCRAResponsibilities> (last accessed July 15, 2009).

[36] The Federal Reserve Board, CRA Performance Ratings, <www.federalreserve.gov/DCCA/CRA/crarate.cfm> (last accessed July 15, 2009).

Non-Compliance with CRA

Low CRA ratings do not result in sanctions or fines.[37] Instead, CRA performance ratings are a factor agencies take into account when an institution makes various applications.[38] For example, the FDIC considers a bank's CRA performance when assessing that institution's application for the establishment of a domestic branch, the relocation of the bank's main office or a branch, the merger, consolidation, or acquisition of assets, and deposit insurance for a newly-chartered institution.[39][40]

III. Fannie Mae and Freddie Mac

A. HUD Goals

The Department of Housing and Urban Development (HUD) has for many years set affordable housing goals for Fannie Mae and Freddie Mac, two Government-Sponsored Enterprises (GSEs) chartered by Congress in 1968[41] and 1970 respectively. This section provides a brief overview of the evolution of the HUD goals and the performance of the GSEs.

B. Legal and Regulatory History of HUD Goals

Prior to 1992, federal law only required that a "reasonable portion" of Fannie Mae and Freddie Mac's mortgage purchases advanced the goal of providing affordable housing to low- and moderate-income families.[42] This amorphous goal was changed upon the adoption of the Federal Housing Enterprise Financial Safety and Soundness Act (FHEFSSA) of 1992. Prior to said statute, HUD promulgated rules

---

[37] *But see* 12 C.F.R. § 25.65 (2009) (OCC may impose sanctions against banks that are in violation of the prohibition against the use of interstate branches primarily for deposit production. Under this provision, if OCC determines that a bank is not reasonably helping to meet the credit needs of the communities served by the bank in the host state, and the bank's statewide loan-to-deposit ratio is less than 50 percent of the host state loan-to-deposit ratio, the agency may order the bank's covered branches to be closed and may not permit the bank to open a new branch unless the bank provides reasonable assurances that it has an acceptable plan under which it will reasonably help to meet the credit needs of the relevant communities.)

[38] The National Community Reinvestment Coalition observed some years ago that, "[a]lthough the federal regulators deny few applications, community activists have used the challenge process to organize and educate members of the community around credit and reinvestment issues. Faced with strong opposition, many banks and thrifts relent to community demands." *See* Chris Bohner, *CRA and HMDA: Tools for Reinvestment*, SWELTERFORCE, NAT'L HOUSING INST., May–June 1995. *See also*, Howard Husock, *The Trillion-Dollar Bank Shakedown That Bodes Ill for Cities*, CITY J. Winter 2000.

[39] Effect of CRA Performance on Applications, 12 C.F.R. § 345.29 (2009).

[40] For recent developments related to the CRA and the mortgage crisis generally, *see* p. 24.

[41] Fannie Mae was originally established as a federal agency in 1938.

[42] U.S. Department of Housing and Urban Development, Response to U.S. Commission on Civil Rights' Interrogatories and Document Requests, Response to Interrogatory Request 8, p. 19 (hereafter referred to as HUD Response to Interrogatories and Document Requests, Interrogatory Request 8), citing Housing and Urban Development Act of 1968, Pub. L. No. 90-448, § 802(ee), 82 Stat. 476, 541 (1968) (regulation of Fannie Mae) and Financial Institutions Reform, Recovery, and Enforcement Act of 1989, Pub. L. No. 101-73, § 731, 103 Stat. 183 (1989) (regulation of Freddie Mac).

requiring "30 percent of GSE conventional mortgage purchase be devoted to mortgages for (1) low- and moderate-income housing; or (2) housing located in central cities."[43]

FHEFSSA

In 1992, Congress established oversight responsibilities for HUD under Title XIII of FHEFSSA.[44] FHEFSSA reaffirmed HUD's regulatory authority to ensure Fannie Mae and Freddie Mac's compliance with their charters. FHEFSSA also mandated specific responsibilities, including:

- Setting the housing goals that require Fannie Mae and Freddie Mac to purchase mortgages made to (i) low- and moderate-income families, (ii) mortgages on properties located in underserved areas, and (iii) mortgages made to very low-income families and low-income families in low-income areas, including mortgages on multifamily properties;
- Monitoring and enforcing Fannie Mae and Freddie Mac's performance in meeting the housing goals;
- Reviewing requests for new program approval submitted by Fannie Mae and Freddie Mac;
- Prohibiting discrimination in Fannie Mae and Freddie Mac's mortgage purchase activities and reviewing and commenting on their underwriting guidelines; and
- Establishing a public use database on Fannie Mae and Freddie Mac's mortgage purchases.[45]

Following the enactment of FHEFSSA, HUD developed an oversight program to carry out these mandates. Specifically, HUD regularly:

> analyze[d] and report[ed] on the GSEs' housing goal performance, housing needs, the marketplace, and the appropriateness of housing goal levels; review[ed] new GSE activities and made determinations about their new program implications; review[ed] the GSEs' underwriting guidelines, including automated underwriting practices, for their fair lending implications; manage[d] performance and risk assessment reviews to verify the accuracy and integrity of data provided by the GSEs to [HUD]; perform[ed] special studies and analyses regarding the GSEs' businesses and their performance in leading the market for affordable lending; create[d] new, and revise[d] existing, GSE reporting requirements as necessary to facilitate informed oversight; and issue[d] new regulations as needed. [HUD] also issue[d] letters and orders regarding its determinations for non-proprietary treatment of GSE mortgage loan data and maintain[ed] the GSE public use database.[46]

---

[43] *Id.* at pp. 19–20, citing 43 Fed. Reg. 36,203 (Aug. 15, 1978) (Fannie Mae housing goals rules) and 56 Fed. Reg. 1,022 (Aug. 16, 1991) (Freddie Mac housing goals rules).

[44] Housing and Community Development Act, Pub. L. No. 102-550, 106 Stat. 4055, 1992 (codified generally at 42 U.S.C. 4501–4641).

[45] U.S. Department of Housing and Urban Development, *Mission Regulation of Fannie Mae and Freddie Mac*, (2003), <http://www.hud.gov/offices/cfo/reports/04estimates/fannieregs.pdf> (last accessed July 15, 2009).

[46] *Id.* HUD's GSE regulatory responsibilities were reduced in July 2008 with the enactment of HERA.

Under the provisions of FHEFSSA, Fannie Mae and Freddie Mac were assessed for the costs of their financial safety and soundness regulation by the Director of the Office of Federal Housing Enterprise Oversight (OFHEO). OFHEO was responsible for ensuring that Fannie Mae and Freddie Mac are adequately capitalized and operating safely.[47]

Pursuant to FHEFSSA, HUD issued lending goals for Fannie Mae and Freddie Mac in 1993, 1995, 2000, and 2004, with the last set including home purchase subgoals.[48] The lending goals and subgoals are described below by year they were issued. Importantly, HUD did not include B, C, and D subprime credit levels in its market share analyses when setting these GSEs' goals because it was expected that "the GSEs were not purchasing mortgages in these markets."[49]

C. *Setting and Meeting the Goals*

Table 1.1
Levels of the Department of Housing and Urban Development's Lending Goals and Subgoals for Government-Sponsored Enterprises, 1996–2007

HOUSING GOALS	YEAR											
	1996	1997	1998	1999	2000	2001	2002	2003	2004	2005	2006	2007
Low- and Moderate-Income Goal	40%	42%	42%	42%	42%	50%	50%	50%	50%	52%	53%	55%
Geographically Targeted (Underserved Area) Goal	21%	24%	24%	24%	24%	31%	31%	31%	31%	37%	38%	38%
Special Affordable Goal	12%	14%	14%	14%	14%	20%	20%	20%	20%	22%	23%	25%
HOME PURCHASE SUBGOALS												
Low- and Moderate-Income Subgoal										45%	46%	47%
Geographically Targeted (Underserved Area) Subgoal										32%	33%	33%
Special Affordable Subgoal										17%	17%	18%

Sources: U.S. Department of Housing and Urban Development, Office of Policy Development and Research, *Profiles of GSE Mortgage Purchases in 1999 and 2000*, April 2002, p. 8 table 1; U.S. Department of Housing and Urban Development, Office of Policy Development and Research, *Profiles of GSE Mortgage Purchases in 2001-2004*, April 2008, p. 9 table 1; U.S. Department of Housing and Urban Development, Office of Policy Development and Research, *Profiles of GSE Mortgage Purchases in 2005-2007*, September 2008, pp. 9–10 tables 1a & 1b.

---

[47] *Id.*

[48] HUD Response to Interrogatories and Document Requests, Interrogatory Request 8 at p. 20 (The goals issued in 1993 were actually categorized as "interim goals.").

[49] HUD Response to Interrogatories and Document Requests, Interrogatory Request 10 at p. 25 ("For purposes of setting individual goal levels, HUD included in its market share analyses [subprime] mortgages generally described as A-minus. These are not considered especially risky mortgages, and the GSEs had asserted that A-minus credit is actually prime credit eligible for more favorable financing. However, HUD excluded the B, C, and D subprime credit levels from its market share analyses, finding that these credit levels were not appropriate markets for the GSEs."). *Id.*

Caption: Between 1996 and 2007, HUD's goals for government-sponsored enterprises increased from 40 to 55 percent of mortgage lending to low- and moderate-income individuals, from 21 to 38 percent of home loans to borrowers in geographically targeted (i.e., underserved) areas, and from 12 to 25 percent to purchasers of special affordable housing. HUD introduced subgoals in 2005 and has increased them slightly since then, with the low-and moderate-income subgoal rising from 45 to 47 percent, the geographically targeted (underserved area) subgoal going from 32 to 33 percent, and the special affordable subgoal from 17 to 18 percent.

Track Record Pre–1995

In 1993, HUD published rules establishing interim goals and subgoals for Fannie Mae and Freddie Mac's mortgage purchases for 1993 and 1994 and the requirements for implementing the goals. In 1993 and 1994, 30 percent of dwelling units financed by Fannie Mae's mortgage purchases were required to be affordable to low- and moderate-income families.[50]

1996–2000 Goals

In 1996, HUD started allowing Fannie Mae and Freddie Mac to get affordable housing credit for buying securities from third parties that included loans to low-income borrowers.[51] This change did not allow B-, C-, or D-rated loan purchases to count toward the affordable housing goals. In 1996, HUD also added for the first time a Special Affordable Multifamily Subgoal.[52]

2001–2003: Goals Significantly Increased

In October 2000, HUD issued its final rule establishing Fannie Mae and Freddie Mac's housing goals levels for 2001 through 2003.[53] For this time period, the Low- and Moderate-Income Housing Goal increased to 50 percent, the Underserved Areas Housing Goal was increased to 31 percent, the Special Affordable Housing Goal was increased to 20 percent, and the Special Affordable Multifamily Subgoal increased to 1 percent of each of Fannie Mae and Freddie Mac's average total mortgages purchased in the 1997-1999 period.[54] Pending the establishment of annual housing goal levels for 2004 and subsequent years, the housing goal levels for each of those years were to be set at 50 percent, 31 percent, and 20 percent respectively. The 2000 rule also: (1) provided for temporary bonus points to Fannie Mae and Freddie Mac for the purchase of mortgages for small multifamily properties and certain single-family owner-occupied rental properties; (2) established a temporary adjustment factor for Freddie

---

[50] *Id.* at p. 20, citing 58 Fed. Reg. 53,048, 53,072 (Oct. 13, 1993).

[51] This policy was subsequently challenged as counter-productive by then Federal Reserve Chairman Alan Greenspan. *See* Bethany McLean, *Fannie Mae's Last Stand*, VANITY FAIR (Feb. 2009), <http://www.vanityfair.com/politics/features/2009/02/fannie–and–freddie200902?> (last accessed July 15, 2009); Peter J. Wallison and Charles W. Calomiris, AM. ENTERPRISE INST., THE LAST TRILLION-DOLLAR COMMITMENT: THE DESTRUCTION OF FANNIE MAE AND FREDDIE MAC (Sept. 2008), <http://www.aei.org/outlook/28704> (last accessed July 15, 2009). "The idea was that subprime lending benefited many borrowers who did not qualify for conventional loans. HUD expected that Freddie and Fannie would impose their high lending standards on subprime lenders." Carol D. Leonnig, *How HUD Mortgage Policy Fed the Crisis*, WASH. POST, June 10, 2008 at A01.

[52] HUD Response to Interrogatories and Document Requests, Interrogatory Request 8 at p. 21.

[53] 65 Fed. Reg. 65,044 (Oct. 31, 2000); HUD Response to Interrogatories and Document Requests, Interrogatory Request 8 at p. 23.

[54] 65 Fed. Reg. 65,044 at 65,086–89 (Oct. 31, 2000); HUD Response to Interrogatories and Document Requests, Interrogatory Request 8 at p. 23.

Mac's purchases of mortgages for certain large multifamily properties; (3) prohibited high-cost mortgages with predatory features from counting towards the Housing Goals; (4) established and clarified counting rules for the goals for certain mortgage loans; (5) established a review process for HUD to determine appropriate Housing Goal treatment for new types of transactions; and (6) made definitional and technical corrections.[55]

2004–2008: Addition of Home Purchase Subgoals

In November 2004, HUD set new Fannie Mae and Freddie Mac housing goals for 2005 through 2008 and, for the first time, established Home Purchase Subgoals for each of the housing goals.[56] The subgoals set a minimum share of home purchases on single-family, owner-occupied properties located in metropolitan areas for each of the goal categories. The purpose of the subgoals was "to encourage the GSEs to facilitate greater financing and homeownership opportunities for families and neighborhoods targeted by the housing goals."[57] The 2004 rule also increased the levels of the housing goals "in nearly equal steps from year-to-year. For example, the Low- and Moderate Income Goal rose from 52 percent in 2005, to 53 percent in 2006, 55 percent in 2007, and 56 percent in 2008."[58] The rule did provide that "if macroeconomic conditions were to change more [than] in previous years, the levels of the goals could be revised to reflect the changed conditions."[59]

Post-Crisis Proposals

A series of accounting and financial problems at Fannie Mae and Freddie Mac, along with financial difficulties at some Federal Home Loan Banks (FHLBs), led many in Congress to conclude that Fannie Mae, Freddie Mac, and the FHLBs needed a stronger regulator. To that end, Congress enacted the Housing and Economic Recovery Act of 2008 (HERA),[60] strengthening government oversight of Fannie Mae and Freddie Mac.[61] The Act established the Federal Housing Finance Agency (FHFA), which replaced OFHEO and HUD as Fannie Mae and Freddie Mac's safety and soundness and mission regulator. Among other things, FHFA has broad authority to require Fannie Mae and Freddie Mac to hold capital above statutory minimum levels, regulate the size and content of their portfolio, and approve new mortgage products.

---

[55] 65 Fed. Reg. 65,044 at 65,086–89 (Oct. 31, 2000); HUD Response to Interrogatories and Document Requests, Interrogatory Request 8 at p. 23.

[56] HUD Response to Interrogatories and Document Requests, Interrogatory Request 8 at p. 23.

[57] *Id.* at p. 24.

[58] *Id.*

[59] *Id.*

[60] Pub.L. No. 110–289, 122 Stat. 2654 (2008).

[61] Congressional Research Service, CRS Report for Congress, *Housing and Economic Recovery Act of 2008*, N. Eric Weiss et al (August 19, 2008), p. 1.

On July 30, 2008, FHFA assumed all oversight responsibility of Fannie Mae and Freddie Mac's compliance with the HUD housing goals set in 2004.[62] Thereafter, on September 6, 2008, FHFA Director James Lockhart appointed FHFA as conservator of Fannie Mae and Freddie Mac.

On December 8, 2008, FHFA sent letters to Freddie Mac and Fannie Mae noting the likelihood of both GSEs meeting the three regulatory housing goals and subgoals established for 2008 based on performance through September 30, 2008.[63] FHFA noted that both Freddie Mac and Fannie Mae were on course to meet only the Underserved Area Goal.[64]

On March 16, 2009, FHFA sent letters to Fannie Mae and Freddie Mac, notifying each of FHFA's final determination that, in the case of Fannie Mae, "there is a substantial probability of failure by Fannie Mae to meet its low- and moderate-income housing goal, special affordable housing goal, and three home purchase subgoals for 2008."[65] The FHFA further noted its determination "that achievement of these goals and subgoals was not feasible."[66]

HERA also revised FHEFFSA to maintain the 2008 goals' levels during 2009, but required the FHFA to review those goals during a 270-day period beginning on the date of enactment.[67] Pursuant to FHFA's review, on May 1, 2009, a proposed rule containing revised 2009 housing goals was posted in the Federal Register.[68] As highlighted in Table 1.2, the proposal would adjust the affordable housing goal and the home purchase subgoal levels for Fannie Mae and Freddie Mac.

---

[62] HUD Response to Interrogatories and Document Requests, Interrogatory Request 8 at p. 24.

[63] Letter from Edward J. DeMarco, Chief Operating Officer and Senior Deputy Officer, Federal Housing Finance Agency, to David Moffett, Chief Executive Officer, Freddie Mac (December 8, 2008); Letter from Edward J. DeMarco, Chief Operating Officer and Senior Deputy Officer, Federal Housing Finance Agency, to Herbert M. Allison, Jr., President and Chief Executive Officer, Fannie Mae (December 8, 2008).

[64] *Id.*

[65] Letter from Edward J. DeMarco, Chief Operating Officer and Senior Deputy Director for Housing Mission and Goals, FHFA, to Herbert Allison, Chief executive Officer, Fannie Mae (March 16, 2009). In its parallel letter to Freddie Mac, FHFA also included the underserved areas goal in this assessment. Letter from Edward J. DeMarco, Chief Operating Officer and Senior Deputy Director for Housing Mission and Goals, FHFA, to John Koskinen, Interior Chief Executive Officer, Freddie Mac (March 16, 2009).

[66] *Id.*

[67] Department of Housing and Urban Development, *Overview of the GSEs' Housing Goal Performance, 2000-2007*, <http://www.huduser.org/Datasets/GSE/gse2007.pdf> (last accessed July 15, 2009).

[68] Federal Housing Finance Agency, 74 Fed. Reg. 20,236 (May 1, 2009) (to be codified at 12 C.F.R. pt. 1282) <http://frwebgate1.access.gpo.gov/cgi-bin/PDFgate.cgi?WAISdocID=166986142392+0+2+0&WAISaction=retrieve> (last accessed July 30, 2009).

Table 1.2
Fannie Mae and Freddie Mac Revised Goals and Subgoals, 2009

Category	Goal/Subgoal	2009 Proposed
Low-mod Income	Goal	51%
Underserved Areas	Goal	37%
Special Affordable	Goal	23%
Low-mod Income	Home Purchase Subgoal	40%
Underserved Areas	Home Purchase Subgoal	30%
Special Affordable	Home Purchase Subgoal	14%
Special Affordable Multifamily	Subgoal: Fannie Mae Freddie Mac	\$5.49 billion \$3.92 billion

Source: Federal Housing Finance Agency, 74 Fed. Reg. 20,236 (May 1, 2009) (to be codified at 12 C.F.R. pt. 1282) <http://frwebgate1.access.gpo.gov/cgi-bin/PDFgate.cgi?WAISdocID=166986142392+0+2+0&WAISaction=retrieve> (last accessed July 30, 2009). FHFA, News Release: FHFA Sends GSE Housing Goals to Federal Register, April 28, 2009.

These levels approximately mirror the prevailing goals from 2004 to 2006.[69]

Starting with 2010, FHFA will establish three single-family home purchase goals, one single-family refinance goal, and one multifamily goal for low-income families.[70]

D. Broad, Continued Legislative Response to the Mortgage Crisis

In March 2009, Representative Eddie Bernice Johnson (D-TX) introduced H.R. 1479, proposing extensive changes to the CRA.[71] The bill proposes the expansion of the CRA to cover a variety of non-bank institutions, including securities and investment services, mortgages and mortgage-related services, insurance services, and credit unions. The bill also requires a reduction of CRA ratings for certain predatory lending or other negative credit practices, and expands coverage areas and opportunities for public comment.[72]

---

[69] FHFA, News Release: FHFA Sends GSE Housing Goals to Federal Register, April 28, 2009.

[70] Fannie Mae 2008 Q2 10-Q Investor Summary at p. 6 (Aug. 8, 2008) Fannie Mae, <http:/www.fanniemae.com/media/pdf/newsreleases/2008_Q2_10Q_Investor_Summary.pdf> (last accessed July 15, 2009).

[71] Community Reinvestment Modernization Act of 2009, H.R. 1479, 111th Cong. (2009).

[72] Many of the changes proposed in the bill reflect recommendations made by leadership of the National Community Reinvestment Coalition in an article appearing in the New York Law School Law Review. *See* John Taylor and Josh Silver, *The Community Reinvestment Act at 30: Looking Back and Looking to the Future*, 53 N.Y.L. SCH. L. REV. 203 (2008/2009). A variety of proposed revisions to the CRA have been made in light of the mortgage crisis. *See Revisiting the CRA: Perspectives on the Future of the Community Reinvestment Act*, A Joint Publication of the Federal Reserve Banks of Boston and San Francisco (February 2009).

In June 2009, OCC, the Federal Reserve, the FDIC, and OTS proposed changes in the CRA regulations for two purposes: 1) to provide express CRA consideration for low-cost education loans to low-income borrowers (as required in the Higher Education Opportunity Act of 2008); and 2) to provide CRA consideration for non-minority and non-women owned financial institutions who undertake activities in cooperation with minority and women owned financial institutions and low-income credit unions (as currently required in the CRA.

In addition to the changes to CRA and the housing goals, volumes of legislative proposals have emerged since the emergence of the mortgage crisis. Bills include the Mortgage Reform and Anti-Predatory Lending Act,[73] the Commission on the Foreclosure and Mortgage Crisis Lending Act,[74] the National Financial Literacy Act,[75] and scores of others addressing the mortgage crisis generally, foreclosure prevention, monitoring of the GSEs, mortgage fraud, and predatory lending.

[73] H.R. 1728, 111th Cong. (2009).

[74] H.R. 1285, 111th Cong. (2009).

[75] H.R. 767, 111th Cong. (2009).

CHAPTER 2: HOMEOWNERSHIP POLICIES: CRITIQUES AND RESPONSE

The bipartisan effort to increase homeownership, together with the evolution of the lending market, resulted in substantial gains. Nonetheless, the policies to affirmatively further homeownership have been criticized by some for weakening underwriting standards and for creating the conditions that led to the present crisis.[1] This viewpoint has been summarized as follows:

> The crisis has its root in the U.S. government's efforts to increase homeownership, especially among minority and other underserved or low-income groups, and to do so through hidden financial subsidies[2] rather than direct government expenditures.
>
> * * *
>
> Instead of a direct government subsidy, say, for down-payment assistance for low-income families, the government has used regulatory and political pressure to force banks and other government-controlled or regulated private entities to make loans they would not otherwise make and to reduce lending standards so more applicants would have access to mortgage financing.[3]

Under this view, government policies seeking to overcome purported discrimination in mortgage lending led to a deterioration in lending standards.

> For almost a decade, beginning in the 1990s, the United States government pursued a policy to increase homeownership. The main tool for achieving the goal was the replacement of historical mortgage underwriting standards with what were called "innovations in mortgage lending" or "flexible underwriting standards." By changing

---

[1] Aside from specific critiques relating to the effects of the CRA on the present mortgage crisis, extensive additional criticism exists with regard to the CRA in general. Such criticism includes contentions that the CRA is not necessary, that it represents unnecessary government interference in lending practices, and/or that it provides an entrée for special interest groups to bring political pressure on lending practices. *See*, *e.g*., Theodore Day and Stan J. Liebowitz, *Mortgage Lending to Minorities: Where's the Bias?*, ECON. INQUIRY, vol. XXXVI (January 1998), at pp. 1–27; Howard Husock, *The Trillion-Dollar Bank Shakedown that Bodes Ill for Cities*, CITY J. Winter 2000; Michelle Minton, *The Community Reinvestment Act's Harmful Legacy: How it Hampers Access to Credit*, COMPETITIVE ENTERPRISE INST., Mar. 20, 2008.

[2] This method of government mandating changes in lending standards has been criticized for shifting risks and burdens from public to private sources, thus minimizing scrutiny and preventing a calculation of the true costs of the policies. *See*, THOMAS SOWELL, THE HOUSING BOOM AND BUST 36 (2009) ("Advocates of 'affordable housing' … seek various ways of either forcing the private sector to charge lower home prices and lower apartment rents, or else they seek to use the taxpayers' money to subsidize housing in one way or another. … They do not seek to *lower* housing costs but to *conceal* housing costs with taxpayer-provided subsidies or with laws that prevent those costs from being expressed in the prices charged.").

[3] PETER J. WALLISON, AM. ENTERPRISE INST., CAUSE AND EFFECT: GOVERNMENT POLICIES AND THE FINANCIAL CRISIS 1 (Nov. 25, 2008), <http:www.aei.org/doclib/20081203_112372NovFSOg.pdf> (last accessed July 16, 2009). *See also* Stan J. Liebowitz, *Anatomy of a Train Wreck; Causes of the Mortgage Meltdown*, NAT'L REV., Oct. 3, 2008 at pp. 34–42 ("The government had been attempting to increase homeownership in the U.S., which had been stagnant for several decades. In particular, the government has tried to increase homeownership among poor and minority Americans. Although a seemingly noble goal, the tool chosen to achieve this goal was one that endangered the entire mortgage enterprise: intentional weakening of the traditional mortgage-lending standards.").

> underwriting standards, the government was able to pursue this policy without using its own money. To get these underwriting standards in place, the government used the bully pulpit, legal and regulatory threats, and political and academic persuasion perhaps more accurately termed as propaganda, to at first coerce the market into bending to its will, and then, in effect, making it an enthusiastic partner in the project.[4]

Such criticism generally acknowledges that, while the CRA might have played a role in the crisis, the CRA was not sufficient to cause a worldwide financial meltdown.[5] As noted by one analyst:

> It would be a foolish overstatement, in my view, to assert that the CRA is somehow the cause or main cause of the current crisis. Exceptionally low interest rates, high levels of available capital, and the advent of mortgage securitization combined – it's clear in retrospect – to spur an overinvestment in housing, and underinvestment in the sort of due diligence which once typified lending. These are huge changes in the financial industry, and I think that they must be considered the key participants of the current situation. But as for the question of whether the CRA is at all linked to our current problems, I would answer in the affirmative.[6]

Instead, it contends that the effort to reduce underwriting standards for minority and low-income individuals inevitably "spread to the wider market – including to prime mortgage markets and to speculative borrowers."[7]

> Although the Community Reinvestment Act had no major immediate impact, over the years its underlying assumptions and provisions provided the basis for ever more insistent pressure on lenders from a variety of government officials and agencies to lend to those

---

[4] Stan J. Liebowitz, Written Statement to the U.S. Commission on Civil Rights, March 20, 2009, p. 1 (hereinafter cited as Liebowitz, Statement).

[5] *See also* WALLISON, CAUSE AND EFFECT at p. 3. Peter J. Wallison, American Enterprise Institute, Debate with the Honorable Richard Posner (Apr. 27, 2009), <http://aei.org/include/pub_print.asp?pubID=297807> (last accessed July 16, 2009) ("CRA did not produce a large number of subprime loans—certainly not enough to cause the current crisis. What it did was start the process of degrading the quality of mortgage loans. The flexible underwriting standards that the government wanted the banks to use really meant lowering down payments, not insisting on income, a steady job, or unblemished credit. The low quality mortgages that were required by CRA—and approved by bank regulators—gradually spread to the rest of [the] mortgage market."); Howard Husock, Written Statement to the U.S. Commission on Civil Rights, March 20, 2009, p. 1 (hereinafter cited as Husock, Statement);

[6] The Community Reinvestment Act and the Subprime Mortgage Crisis: Is There a Connection, edited transcript, Hudson Institute's Bradley Center for Philanthropy and Civic Renewal and Center for Housing and Financial Markets, Testimony of Howard Husock at p. 10 (October 23, 2008).

[7] WALLISON, CAUSE AND EFFECT at p. 3 (Wallison elaborated: "Once these standards were relaxed – particularly allowing loan-to-value ratios higher than the 20 percent that had previously been the norm – they spread rapidly to the prime market and to subprime markets where loans were made by lenders other than insured banks."). *See also* Liebowitz, *Anatomy of a Train Wreck* at p. 40 ("[A]lthough the original mortgage innovations were rationalized for low- and middle-income buyers, once this sloppy thinking had taken hold it is naïve to believe that this decade-long attack on traditional underwriting standards would not also lead to more relaxed standards for higher-income borrowers as well.").

> whom politicians and bureaucrats wanted them to lend to, rather than to those that lenders would have chosen to lend to on the basis of the lenders' own experience and expertise.[8]
>
> * * *
>
> [E]ven though racial bias charges provided much of the initial impetus for greater federal government involvement in private mortgage lending decisions, once federal regulatory agencies became involved that involvement spread far beyond issues of race, and the policies imposed required a lowering of mortgage loan approval standards across the board, to people of all races.[9]

Similar criticism exists with regard to the HUD lending goals and the alleged effect they had on Fannie Mae and Freddie Mac's lending practices.[10] While the criticism of weakened underwriting standards is made with equal force as to the HUD lending goals,[11] additional factors are said to exist with regard to the practices of Fannie Mae and Freddie Mac. This analysis posits that, as Fannie Mae and Freddie Mac lost market share to private label securitization (i.e., Wall Street), Congress put increased pressure on them to increase low- and moderate-income loans.[12] It is contended that this combination led Fannie

---

[8] Sowell, The Housing Boom and Bust at pp. 36–37.

[9] *Id.* at p. 38. *But see* The Community Reinvestment Act and the Subprime Mortgage Crisis: Is There a Connection, edited transcript, Hudson Institute's Bradley Center for Philanthropy and Civic Renewal and Center for Housing and Financial Markets, Testimony of Barry Zigas at p. 13 (Oct. 23, 2008). In his testimony, Mr. Zigas argued that the issue of causation between the CRA and the weakened lending standards could not be proven. He stated:

> I do get off the bus, though, when the analogy is extended to saying, well, CRA was in place; bad things ended up happening; ergo CRA is a contributor to the problem. I suppose that's true, but then I will posit that gravity is also a contributing factor to the subprime mortgage crisis. After all, everything that goes up must come down; we're all subject to gravity; and it has been there ever since we've been doing lending, so it must have something to do with this. The real issue here is to try to disaggregate the effects. We should ask, if it were a contributing factor to the current crisis, where is the evidence for it?

[10] *See* Carol D. Leonnig, *How HUD Mortgage Policy Fed the Crisis*, WASH. POST, June 10, 2008, at A01:

> In 2001, HUD researchers warned of high foreclosure rates among subprime loans. "Given the very high concentration of these loans in low-income and African-American neighborhoods, the growth in subprime lending and resulting very high levels of foreclosure is a real cause for concern," an agency report said. But by 2004, when HUD next revised the goals, Freddie and Fannie's purchases of subprime-backed securities had risen tenfold. Foreclosure rates also were rising.

[11] *See* Husock, Statement at pp. 4–5 ("Beginning in 1992, the Department of Housing and Urban Development pushed Fannie and Freddie to buy loans on criteria other than credit-worthiness."). *See also* Michael Shermer, *Irrational Economic Man*, CITY J. Jan. 11, 2009; Carol D. Leonnig, *How HUD Mortgage Policy Fed the Crisis*, WASH. POST, June 10, 2008.

[12] *See* WALLISON, CAUSE AND EFFECT at pp. 4–5:

> When the history of this era is written, students will want to understand the political economy that allowed Fannie and Freddie to grow without restrictions while producing larger profits for shareholders and management but no apparent value for the American people. The answer is the affordable housing mission that was added to their charters in 1992, which-like the CRA-permitted Congress to subsidize LMI [low and moderate income] housing without appropriating any funds. As long as Fannie and Freddie could credibly contend that they were advancing the interests of LMI homebuyers, they could avoid new regulation by Congress-especially restrictions on the accumulation of mortgage portfolios, totaling approximately $1.5 trillion by 2008, that accounted for most of their profits. They could argue to Congress that if the mortgage portfolios were constrained by regulation, they could not afford to subsidize affordable

Mae and Freddie Mac to increase their portfolios of subprime private label mortgages.[13] One academic characterized Fannie Mae and Freddie Mac's subprime purchases in the first half of the decade as follows:

> Between 2000 and 2005, Fannie and Freddie met those goals every year, funding hundreds of billions of dollars worth of loans, many of them subprime and adjustable-rate loans, and made to borrowers who bought houses with less than 10% down.
>
> Fannie and Freddie also purchased hundreds of billions in subprime securities for their own portfolios to make money and to help satisfy HUD affordable housing goals. Fannie and Freddie were important contributors to the demand for subprime securities.[14]

This criticism contends that, as Fannie Mae and Freddie Mac increased their purchase of subprime loans, a false impression was created that such loans carried little risk, which greatly influenced the lending and investment practices involving non-GSE entities.[15] This argument has been summarized as follows:

> housing. In addition, the political sophistication of Fannie Mae's management enabled the company to serve the interests of key lawmakers who could and did stand in the way of the tougher regulation that might have made the current crisis far less likely.

[13] Kathleen Day, *Villains in the Mortgage Mess? Start at Wall Street. Keep Going.*, WASH. POST, June 1, 2008, at B01:

> For the most part, they [Fannie Mae and Freddie Mac] didn't buy the most abusive subprime mortgages from lenders because the loans didn't meet their standards. But they did buy private-label subprime bonds for their own investment portfolios to boost profits. From 2004 through 2006, these Congressionally-chartered companies bought a third of the $1.6 trillion in private-label bonds that Wall Street firms issued. This helped legitimize the market, giving pension funds and foreign governments additional (albeit false) comfort that these securities were safe. Bush regulators have also allowed Fannie and Freddie to count these securities toward federally set goals for encouraging mortgage lending to low-income borrowers.

See also PETER J. WALLISON AND CHARLES W. CALOMIRIS, AM. ENTER (Sept. 30, 2008), <http://www.aei.org/docLib/20080930_Binder1.pdf> (last accessed July 16, 2009) (hereinafter cited as WALLISON AND CALOMIRIS, AEI, THE LAST TRILLION DOLLAR COMMITMENT).

[14] Russell Roberts, *How Government Stoked the Mania*, WALL ST. J., Oct. 3, 2008, at A21. *See also* SOWELL, THE HOUSING BOOM AND BUST at pp. 57–58 ("The development of lax lending standards, both by banks and by Fannie Mae and Freddie Mac standing behind the banks, came *not* from a lack of government regulation and oversight, but precisely as a *result* of government regulation and oversight, directed toward the politically popular goal of more "home ownership" through "affordable housing," especially for low-income home buyers. These lax lending standards were the foundation for a house of cards that was ready to collapse with a relatively small nudge.").

[15] *See* Day, *Villains in the Mortgage Mess*; Zachary A. Goldfarb, *Internal Warnings Sounded on Loans at Fannie, Freddie*, WASH. POST, Dec. 9, 2008, at D01; ([D]ocuments suggested that Fannie and Freddie knew they were playing a role in shaping the market for some types of risky mortgages. An e-mail to Mudd [of Fannie Mae] in September 2007 from a top deputy reported that banks were modeling their subprime mortgages to what Fannie was buying."); Stuart Taylor, Jr., *$1 Trillion of Blame*, LEGAL TIMES, Oct. 20, 2008 ("[W]hy would investment banks take foolish risks with their own money, as well as that of investors, just because Fannie and Freddie were doing so? In an interview, [Peter] Wallison theorizes that the companies wrongfully assumed that these must be sound investments because the leading experts on the mortgage market, Fannie and Freddie, with their vast databases and sophisticated computer programs, thought so. But unbeknownst to the investment banks, the experts at Fannie and Freddie knew very well that their bosses were taking reckless risks.").

> In a very real sense, then, competition from Fannie and Freddie beginning in late 2004 caused both groups to scrape the bottom of the barrel – Fannie and Freddie in order to demonstrate to Congress their ability to increase support for affordable housing, and the private-label issuers trying to maintain their market share against the GSEs' increased demand for subprime and Alt-A product. Thus, the gradual decline in lending standards that began with the revised CRA regulations in 1993 and continued with the GSEs' attempts to show Congress that they were meeting their affordable housing missions, came to dominate mortgage lending in the United States.[16]

I. Response to the Alleged Role of the CRA and HUD Lending Goals in the Mortgage Crisis

Each of the four agencies responsible for CRA examination (OCC, OTS, FDIC and the Federal Reserve) has stated publicly its belief that the CRA was not responsible for the current mortgage crisis. Deputy Comptroller for Community Affairs Barry R. Wides has stated, "[l]et me start off by assuring you, unequivocally, that CRA is not the culprit behind the abuses in subprime mortgage lending nor the broader credit quality issues in the marketplace."[17] In support of this belief, the various agencies cited three main factors.[18] First that the CRA was enacted over 30 years ago and its last major change was over a decade ago. It is argued that, if the CRA was the impetus for relaxed underwriting standards, the crisis should have happened a long time ago. Second, the agencies point to the small number of CRA originations, which have been decreasing over time, as well as the comparable performance of CRA subprime loans to non-CRA subprime loans. Third, the agencies point out that the lending institutions that made the majority of subprime loans are not CRA-covered institutions.[19]

On the issue of timing – the passage of CRA in 1977 versus the more recent emergence of the subprime mortgage coverage – a Federal Reserve memorandum notes that, since 1995,

> there has been essentially no change in basic CRA rules or the enforcement process that can be reasonably linked to subprime lending activity. This fact weakens the link between the CRA and the current crisis since the crisis is rooted in the poor performance of mortgage loans made between 2004 and 2007. [20]

---

[16] WALLISON, CAUSE AND EFFECT at p. 6.

[17] Barry D. Wides, Deputy Comptroller for Community Affairs, Written Statement to the U.S. Commission on Civil Rights, March 20, 2009.

[18] Each of these arguments was challenged by Stan Liebowitz in his written testimony submitted to the Commission. *See* Liebowitz, Statement.

[19] Further elaborating, OTS stated that "foreclosure filings have increased at a faster pace in middle- or higher-income areas than in lower-income areas, which are the focus of CRA requirements," and that, in fact, "CRA may have deterred irresponsible lending." OTS, "Statement on the Role of the Community Reinvestment Act in the Current Mortgage Credit Crisis" (2009).

[20] Memorandum from Glenn Canner and Neil Bhutta to Sandra Braunstein, Director, Consumer & Community Affairs Division, Federal Reserve, Staff Analysis of the Relationship between the CRA and the Subprime Crisis, p. 2 (Nov. 21, 2008).

Furthermore, the Federal Reserve noted that the majority of the loans alleged to have contributed to the mortgage crisis were not made by CRA-covered lenders.

> [O]nly 6 percent of all the higher-priced [subprime] loans were extended by CRA-covered lenders to lower-income borrowers or neighborhoods in their CRA assessment areas, the local geographies that are the primary focus for CRA evaluation purposes. This result undermines the assertion by critics of the potential for a substantial role for the CRA in the subprime crisis. In other words, the very small share of all higher-priced loan originations that can reasonably be attributed to the CRA makes it hard to imagine how this law could have contributed in any meaningful way to the current subprime crisis. [21]

The Comptroller of the Currency John C. Dugan voiced a similar opinion in late 2008, saying that he "categorically disagrees with suggestions that the Community Reinvestment Act is partly responsible for the ongoing credit crisis."[22]

> Indeed, the lenders most prominently associated with subprime mortgage lending abuses and high rates of foreclosure are lenders not subject to [the] CRA … A recent study of

---

[21] Randall S. Kroszner, Governor, Bd. of Governors of the Fed. Reserve System, Address at the Confronting Concentrated Poverty Policy Forum: The Community Reinvestment Act and the Recent Mortgage Crisis (Dec. 3, 2008). This theme was expanded upon in the November 21, 2008 memorandum:

> [T]he CRA does not cover independent nonbank lending institutions, such as mortgage and finance companies and credit unions. In other words, these institutions are not directly affected by CRA incentives
>
> …
>
> Analysis of 2006 Home Mortgage Disclosure Act (HMDA) data indicates that two-thirds of mortgage loans (first-lien home purchase and refinance loans for site-built properties) are entirely unrelated to CRA; these loans were extended to middle- or higher-income borrowers or to borrowers located outside of lower-income neighborhoods. These data also indicate that only ten percent of all loans are "CRA-related" — that is, lower-income loans made by banks and their affiliates in their CRA assessment areas.
>
> More important for this discussion is CRA's relationship to subprime mortgage lending. … [I]n 2005 and 2006, the peak years of subprime volume, independent mortgage companies (institutions not covered by the CRA) accounted for about half of all higher-priced loans (our proxy for subprime lending derived from HMDA data).
>
> Also, 57 percent of all higher-priced loans in 2006 were effectively unrelated to CRA because they were made to non-lower-income borrowers or neighborhoods Most importantly, only 6 percent of all higher-priced loans in 2006 were made by CRA-covered institutions or their affiliates to lower-income borrowers or neighborhoods in their assessment areas. As noted, CRA performance evaluations focus on lower-income lending in CRA assessment areas.
>
> To the extent that banking institutions chose not to include their affiliates' lending in their CRA examinations, the 6 percent figure overstates the volume of higher-priced lower-income lending that CRA examiners would have counted.

Memorandum from Glenn Canner and Neil Bhutta to Sandra Braunstein, Director, Consumer & Community Affairs Division, Federal Reserve, Staff Analysis of the Relationship between the CRA and the Subprime Crisis, pp. 2–3 (Nov. 21, 2008) (emphasis in original).

[22] John C. Dugan, Comptroller of the Currency, *Comptroller Says CRA Not Responsible for Subprime Lending Abuses*, REUTERS, Nov. 19, 2008.

> 2006 Home Mortgage Disclosure Act data showed that banks subject to CRA and their affiliates originated or purchased only six percent of the reported high cost loans made to lower-income borrowers within their CRA assessment areas.[23]

Finally, as stated by Federal Reserve Governor Randall S. Kroszner:

> [T]wo key points emerge from all of our analysis of the available data. First, only a small portion of subprime mortgage originations are related to the CRA. Second, CRA- related loans appear to perform comparably to other types of subprime loans. Taken together, as I stated earlier, we believe that the available evidence runs counter to the contention that the CRA contributed in any substantive way to the current mortgage crisis. [24]

Another authority noted that the "dramatic increase in the share of originations by non-CRA regulated institutions … was coincident with the rise in the importance of securitization and the increasing role of subprime lending as independent mortgage companies were not subject to CRA regulations."[25]

---

[23] *Id.* This argument was challenged during the Commission's briefing on this topic. During his testimony, Stan Liebowitz raised an analogy to explain how even a small number of CRA loans could infect the system at large:

> To put things in perspective, it is helpful to use a simple analogy. Let's assume that some owners of high-performance cars form a coalition with the goal of eliminating traffic lights and speed limits. Let's also assume that they represent only a small portion of drivers but, nevertheless, are successful at changing the laws. We could say, in other words, that driving standards had been weakened.
>
> Then, with no traffic lights and no traffic speed limits, all hell breaks loose on the roads. Traffic jams are everywhere. Accidents occur, and injuries skyrocket.
>
> Let's assume the economy is going to a standstill by the dysfunctional transportation system. Naturally the government would attempt to figure out who caused t his problem.
>
> The owners of the high-performance vehicles can point out, those who belong to that group, that their vehicles make up only a small proportion of all the vehicles stuck in traffic jams. And, therefore, it can't be that the traffic jams are due to them or their vehicles.
>
> Further, they can point out that their members incur fatalities at no higher rates than other drivers of high-performance cars that do not belong to their coalition. They can claim, therefore, that their group has nothing to do with the traffic problems that have befallen the country.
>
> This is essentially the argument that has been made by those who are trying to deflect attention away from the true problem, which is the reduction in lending standards, and, instead, saying it has to do with just the CRA.

U.S. Commission on Civil Rights, Briefing Transcript of March 20, 2009, pp. 56–57. Available at <http://www.usccr.gov>.

[24] Randall S. Kroszner, Governor, Bd. of Governors of the Fed. Reserve System, Address at the Confronting Concentrated Poverty Policy Forum: The Community Reinvestment Act and the Recent Mortgage Crisis (Dec. 3, 2008).

[25] Marsha Courchane, Written Statement to the U.S. Commission on Civil Rights, March 20, 2009, p. 6. (Ms. Courchane is Vice President of Charles River Associates and has extensive experience in the areas of mortgage and consumer lending.). *See also* NATIONAL COMMISSION ON FAIR HOUSING AND EQUAL OPPORTUNITY, THE FUTURE OF FAIR HOUSING: REPORT OF THE NATIONAL COMMISSION ON FAIR HOUSING AND EQUAL OPPORTUNITY § 5 (December 2008); CENTER FOR AM. PROGRESS, IDEA OF THE DAY: THE COMMUNITY REINVESTMENT ACT DIDN'T CAUSE THE FINANCIAL CRISIS, Oct. 3, 2008, <http://www.americanprogress.org/issues/ideas/2008/10/100308.html> (last accessed July 17, 2009); James H. Carr and David Berenbaum, Written Statement to the U.S. Commission on Civil Rights, March 20, 2009, p. 7.

Others have indicated a similar viewpoint with regard to HUD's affordable housing lending goals, contending that the effort to increase homeownership did not cause the crisis in mortgage lending. For example, John Weicher, Director of the Center for Housing and Financial Markets at the Hudson Institute and former HUD Assistant Secretary for Housing, contends that the increases in affordable housing goals had little impact on Fannie Mae and Freddie Mac's subprime mortgage purchases.

> There is … evidence on the extent to which the GSEs were buying subprime mortgages, both before and after the 2005 rule went into effect. This evidence indicates that the affordable housing goals had little if any impact on GSE activity in these markets. Instead, it appears that the GSEs were responding to the same factors in the mortgage market as other lenders.[26]

Weicher asserted:

> The GSEs were not alone … Beginning in 2002, other lenders were taking more risk by relaxing underwriting standards. These lenders – both portfolio lenders such as commercial and community banks, and issuers of private mortgage pools – began taking more risk in 2002 and continued to do so until 2005. These lenders were not subject to the affordable housing goals, but they behaved the same way as the GSEs.[27]

This position is bolstered by the argument that factors other than the HUD lending goals more directly affected the decision by Fannie Mae and Freddie Mac to increase their share of the subprime market. These independent factors included the effort to increase profits, the need to meet increased Congressional pressure to expand affordable lending as the housing market began to slow down, and the desire to escape the shadow of accounting scandals that hit both Fannie Mae and Freddie Mac in 2003 and 2004.[28]

---

[26] John Weicher, Written Statement to the U.S. Commission on Civil Rights, March 20, 2009. p. 4 (hereafter referred to as Weicher, Statement). *See also* Bethany McLean, *Fannie Mae's Last Stand*, VANITY FAIR, February 2009, <http://www.vanityfair.com/politics/features/2009/02/fannie-and-freddie200902?> (last accessed July 15, 2009) ("Although both companies justified their purchases of risky loans based on their need to meet HUD's affordable housing goals, former Fannie employers say that, while the P.L.S. [private label securities] purchases did aid in meeting the goals… the Alt-A loans did not. In other words, Fannie dove into Alt-A not because of its mission but because of its bottom line – and because its executives feared that Fannie would become irrelevant if it continued to say no to this brave new world.").

[27] Weicher, Statement at p. 6. Weicher further asked:

> If the affordable housing goals don't account for the GSEs' behavior, what does? The best explanation is the simplest. The GSEs badly misjudged the risk of subprime and Alt-A mortgages. So did other lenders. Indeed, the GSEs were by no means the first lenders to run into problems with their non-prime portfolios; HBSC and New Century were front-page news in February 2007. But the GSEs, because they were bigger and required to hold less capital, took the biggest risks and had the most spectacular problems.

Id. *See also* Jeffrey Toobin, *Barney's Great Adventure*, NEW YORKER, Jan. 12, 2009, at p. 40 ("Fannie and Freddie were contributors to the bubble, but they came late in the really bad loans, after the private issuers like Merrill and Citigroup," Dean Baker, the co-director of the Center for Economic and Policy Research, in Washington, said.").

[28] *See* WALLISON AND CALOMIRIS, AEI, THE LAST TRILLION-DOLLAR COMMITMENT. S*ee also* Goldfarb, *Internal Warnings Sounded on Loans at Fannie, Freddie* ("At Fannie Mae, top executives were told it was necessary to develop 'underground' efforts to buy subprime mortgages because of competitive pressure, although there were growing risks and borrowers often

Following the accounting scandals, Daniel Mudd was named Chief Executive of Fannie Mae. The pressures he faced at the time have been summarized as follows:

> [B]y the time Mr. Mudd became Fannie's Chief Executive in 2004, his company was under siege. Competitors were snatching lucrative parts of its business. Congress was demanding that Mr. Mudd help steer more loans to low-income borrowers. Lenders were threatening to sell directly to Wall Street unless Fannie bought a bigger chunk of their riskiest loans.
>
> So Mr. Mudd made a fatal choice. Disregarding warnings from his managers that lenders were making too many loans that would never be repaid, he steered Fannie into more treacherous corners of the mortgage market, according to executives.
>
> For a time, that decision proved profitable. In the end, it nearly destroyed the company and threatened to drag down the housing market and the economy.[29]

In an interview, Mr. Mudd stated:

> "Fannie Mae faced the danger that the market would pass us by," he said. "We were afraid that lenders would be selling products we weren't buying and Congress would feel like we weren't fulfilling our mission. The market was changing, and it's our job to buy loans, so we had to change as well."[30]

While Fannie Mae and Freddie Mac's expansion of subprime loan purchases was aided by the 1995 HUD policy allowing them to count such purchases toward their affordable housing credit,[31] it has been

---

didn't understand the terms of the loans, documents show."). Charles Duhigg, *At Freddie Mac, Chief Disregarded Warning Signs*, N.Y. TIMES, Aug. 5, 2008 ("The companies were constantly under [Congressional] pressure to buy riskier mortgages. Once, a high-ranking Democrat telephoned executives and screamed at them to purchase more loans from low-income borrowers, according to a Congressional source.").

[29] Charles Duhigg, *Pressured to Take More Risk, Fannie Reached Tipping Point*, N.Y. TIMES, Oct. 5, 2008, at A1. Freddie Mac was feeling similar pressure. *See* Duhigg, *At Freddie Mac, Chief Disregarded Warning Signs*; Goldfarb, *Internal Warnings Sounded on Loans at Fannie, Freddie* ("As Mudd's [at Fannie Mae] and Syron's [at Freddie Mac] decisions have been called into question, they have described their push into these new areas of the mortgage business as an inevitable consequence of dueling mandates to support affordable housing and maximize profit for shareholders.").

[30] Duhigg, *Pressured to Take More Risk, Fannie Reached Tipping Point* (This article also included the following purported comments from Angelo R. Mozilo, the head of Countrywide Financial, at the time the nation's largest mortgage lender: "You're becoming irrelevant," Mr. Mozilo told Mr. Mudd, according to two people with knowledge of the meeting who requested anonymity because the talks were confidential. In the previous year, Fannie had already lost 56 percent of its loan-reselling business to Wall Street and other competitors. "You need us more than we need you," Mr. Mozilo said, "and if you don't take these loans, you'll find you can lose much more."). *See also* WALLISON AND CALOMIRIS, AEI, THE LAST TRILLION-DOLLAR COMMITMENT ("[T]he GSEs sold out the taxpayers by taking huge risks on substandard mortgages, primarily to retain Congressional support for the weak regulation and special benefits that fueled their high profits and profligate executive compensation. As if that were not enough, in the process, the GSEs' operations promoted a risky subprime mortgage binge in the United States that has caused a worldwide financial crisis.").

[31] The policy is discussed in Chapter 1.

argued that their pursuit of subprime loans had more to do with profitability than increasing affordable housing.[32]

This argument is supported by the fact that, to a large degree, the expansion of Fannie Mae and Freddie Mac into subprime markets was in the form of increasing their own investment portfolios with the purchase of private-label bonds from Wall Street firms.[33] This policy was questioned at the time as both creating excessive risk as well as failing to actually increase affordable home lending.[34]

As one author described the process:

> [Fannie and Freddie] began to repurchase their own mortgage-backed securities, and to buy similar securities that were created by Wall Street without the G.S.E. guarantee, and hold them in a portfolio. Then Fannie and Freddie pocketed the difference – what Greenspan called "the big fat gap" – between what the mortgages yielded and the companies' own cost of borrowing funds. This was an immensely profitable business: Wall Street analysts estimated that it provided up to three-fourths of Fannie's and Freddie's earnings … Critics, most notably Alan Greenspan, argued that the portfolio wasn't worth any risk at all because it did nothing to put people in homes and existed only to make money for the companies' executives and shareholders.[35]

Put another way, it is argued that the decision by Fannie Mae and Freddie Mac to increase their portfolio of subprime holdings was a back door way of meeting housing affordability goals while maximizing profits. The only problem was that neither of these goals actually increased affordable home lending. As stated by one expert:

> [Alan] Greenspan has suggested that their most profitable activity – holding portfolios of mortgages and MBS [mortgage-backed securities] – was the activity that created the greatest risk, and three Federal Reserve economists had concluded that the GSEs' activities did not actually reduce mortgage interest rates. It was easy to see at this point

---

[32] McLean, *Fannie Mae's Last Stand* ("Although both companies resisted due to their worries about the riskiness of the new products, eventually senior executives disregarded internal warnings, because the lure of big profits was too great. 'We're rushing to get back into the game,' Mudd told analysts in the fall of 2006. 'We will be there.'"); Goldfarb, *Internal Warnings Sounded on Loans at Fannie, Freddie* ("Despite… concerns [over subprime and Alt-A loans], Fannie continued to push into this new market. A business presentation in 2005 expressed concerns that unless it didn't, Fannie could be relegated to a 'niche' player in the industry. Mudd later reported in a presentation that Fannie moved into this market 'to maintain relevance' with big customers who wanted to do more business with Fannie, including Countrywide, Lehman Brothers, IndyMac and Washington Mutual.").

[33] *See* Day, *Villains in the Mortgage Mess? Start at Wall Street. Keep Going* ("For the most part, [Fannie Mae and Freddie Mac] didn't buy the most abusive subprime mortgages from lenders because the loans didn't meet their standards. But they did buy private-label subprime bonds for their own investment portfolios to boost profits. From 2004 through 2006, these Congressionally chartered companies bought a third of the $1.6 trillion in private-label bonds that Wall Street firms issued. This helped legitimize the market, giving pension funds and foreign governments additional (albeit false) comfort that these securities were safe.").

[34] McLean, *Fannie Mae's Last Stand* ("In the end, it was Fannie executives who made a business decision to stake their future on risky mortgages that had nothing to do with helping people own homes.").

[35] *Id.*

> that their political risk was rising quickly. The case for continuing their privileged status had been severely weakened. The only element of their activities that had not come under criticism was their affordable housing mission, and it appears the GSEs determined at this point to play that card as a way of shoring up their political support in Congress.[36]

II. Other Causes

Regardless of the perceived influence of the CRA and the HUD lending goals, there can be no question that a variety of additional factors played a role in the increase in homeownership, the relaxation of underwriting standards, and the recent crisis in the mortgage markets.[37] These factors were not static. That is to say, circumstances changed over time, as did market conditions. Such factors included the availability of various kinds of credit as well as the manner in which such credit was made available on the secondary market.

In reviewing homeownership levels over several decades, one report noted the following:

> What sparked the decade-long homeownership boom was … the improved affordability brought by lower interest rates and the flat home prices in the wake of the 1990-1991 recession. That downturn was quickly followed by the longest economic expansion since World War II and unusually strong, broad-based income growth. During this period, Congress and regulators also leaned on financial institutions to step up lending in low-income and minority neighborhoods. Deeply important, widespread adoption of automatic underwriting tools in the latter part of the 1990s allowed many more borrowers to qualify for prime loans while adding little credit risk.[38]

An examination of lending practices from 2001 to 2006, during which the housing market rapidly expanded, crested and then began its decline, reveals two distinct stages.[39] The first period was from 2001 to 2003, a period during which most of the mortgage origination involved fixed rate loans:

> Over these three years, the vast majority of mortgages originated were loans with fixed rate mortgages provided to borrowers with relatively strong credit histories. The FRM [fixed rate mortgage] share of mortgage applications averaged 84 percent from 2001 to 2003, while

---

[36] *See* WALLISON AND CALOMIRIS, AEI, THE LAST TRILLION-DOLLAR COMMITMENT.

[37] It has been argued that these additional factors independently could affect underwriting standards*. See, e.g*., Paul S. Calem, Marsha J. Courchane and Susan M. Wachter, *Sustainable Homeownership*, paper presented at Housing After the Fall: Reassessing the Future of the American Dream, p. 19 (March 19, 2009):

> [T]he rapid expansion of subprime and Alt-A lending and originations during 2004-2006 was coincident with rapidly accelerating house price appreciations and some declines in homeownership rates. In this context, nonprime lending and non-traditional products were not serving to broaden homeownership. Rather rapid house price appreciation may have encouraged a loosening of credit standards.

[38] JOINT CTR. FOR HOUS. STUDIES OF HARV. U. THE STATE OF THE NATION'S HOUSING 17 (2008).

[39] As noted by one authority, financial booms often occur in stages: "Speculation often develops in two stages. In the first, sober stage of investment, households, firms, investors, or other actors respond to a displacement in a limited and rational way; in the second, capital gains play a dominating role." CHARLES KINDLEBERGER, MANIAS, PANICS AND CRASHES: A HISTORY OF FINANCIAL CRISES 131-32 (1978).

> subprime mortgage originations (i.e., loans made to borrowers with relatively weak credit history or loans made by lenders that specialize in such lending) accounted for only about 7 percent of total single family mortgage market activity over the three-year period … because most of the loans originated from 2001 to 2003 were prime, traditional, fixed-rate mortgages, Fannie Mae, Freddie Mac and Ginnie Mae dominated the secondary mortgage market activity (i.e., issuance of mortgage backed securities (MBS)) during this period.[40]

By 2004, however, residential real estate had appreciated greatly. The increased cost of housing required loans in larger amounts which, in turn, resulted in greater risk in lending. As a result, lending practices changed:

> [T]he FRM share of mortgage applications averaged 69 percent from 2004 to 2006 (down from an average of 84 percent over the prior three year period). In addition, the subprime share of single family originations rose steadily from eight percent in 2003 to 20 percent in 2006, while the Alt-A share increased from just two percent to 13 percent over the same period. … [A]fter 2003, due to somewhat higher mortgage rates and very rapid home appreciation, housing affordability declined steadily until falling to a 21-year low in 2006. This decline in affordability led the mainstreaming of many of the nontraditional mortgage products that became quite popular among lenders and borrowers beginning in 2004. Relative to traditional FRMs, these non-traditional products offered significantly lower initial monthly payments that made it possible for borrowers to purchase homes that they might not have otherwise been able to afford (particularly in areas experiencing extremely rapid increases in home prices).[41]

Throughout this time period, the growth of securitization greatly influenced lending practices.[42] The process of securitization has been described as follows:

> Securitization is the financial technology that integrates the market for residential mortgages with the capital markets. In securitization, investment banks take pools of home loans, carve up the cash flows from those receivables, and convert the cash flows

---

[40] Marsha J. Courchane and Peter M. Zorn *Dawning of a New Age: Examination for Discrimination in Lending*, BANKING & FIN. SERVICES POL'Y REP., October 2008, p. 3.

[41] *Id.* at p. 4. S*ee also* Dina ElBoghdady and Sarah Cohen, *The Growing Foreclosure Crisis*, WASH. POST, Jan. 17, 2009 at A1 ("For a brief time in 2005, the housing market showed signs of cooling nationwide and interest rates edged up. Lenders reacted by reaching out to ever riskier borrowers with more subprime and other exotic loans to keep the home-buying frenzy going, said Howard Shapiro, an analyst at investment bank Fox-Pitt Kelton."); GILLIAN TETT, FOOL'S GOLD 126 (2009) ("The business had fallen victim to a vicious cycle: banks and other lenders were issuing more and more mortgages, which were riskier and riskier, so that those loans could be repackaged into more and more CDOs [collateralized debt obligations] in order to make up for the declining profit margins."); Gretchen Morgenson, *How the Thundering Herd Faltered and Fell*, N.Y. TIMES, Nov. 9, 2008, at BU1.

[42] *See* Peter M. Zorn and Marsha J. Courchane, *Mortgage Market Players and Products*, paper presented at Housing After the Fall: Re-assessing the Future of the American Dream, p. 3 (Mar. 17, 2009).

> [T]he secondary market allows lenders to pool loans from anywhere in the country and sell the securities through the secondary market. This increases the liquidity of lenders' assets, dramatically reduces localized variations in lending rates and the availability of credit, and reduces credit risks through geographic diversification. The growth of the secondary market, therefore, encouraged economies of scale, as well as the growth of nondepository institutions.

> into bonds that are secured by the mortgages. The bonds are variously known as residential mortgage-backed securities (RMBS) or asset-backed securities (ABS).
>
> ***
>
> [T]he investment bank for the issues carves the principal and interest payments into tranches of bonds. Then, rating agencies gauge the credit risk of each tranch by comparing the loan pool's characteristics with historical data and forecasting the tranch's performance.[43]

The process of securitization, and its applicability to mortgage-backed securities, greatly increased as mortgage interest rates dropped. While the return on other investments, such as stocks and government bonds, decreased, mortgage-backed securities, especially those based on riskier subprime mortgages, offered higher rates of return.[44] As noted by one author:

> The American housing market had benefited hugely from the low interest rates Alan Greenspan was holding to, and the rapidly mounting piles of mortgage loans were fertile fodder for the CDO [collateralized debt obligation] machine. This was especially true because so many of the new mortgages were relatively high risk, which allowed the banks to offer extremely attractive returns….For returns-hungry investors, subprime-mortgage-based CDOs were gold dust.[45]

Two factors came together to make subprime loans more attractive to investors. First, it was believed that financial markets had created sufficient safeguards to protect investors.[46] While subprime loans traditionally have provided for greater interest rates, due to higher rates of default, it was perceived that

---

[43] Audrey Strauss, *Turning a Blind Eye: Wall Street Finance of Predatory Lending*, 75 FORDHAM L. REV. 2039, 2045-46 (2007).

[44] *Id.* at n.78. *See also* Jill Drew, *Frenzy: When the Housing Market Began to Tank in 2005, Wall Street Ran Through the Yellow Light of Caution and Created Even Riskier Investments – and Washington had no Mechanism for Finding out what was Going on*, WASH. POST, Dec. 16, 2008, at A1; TETT, FOOL'S GOLD at p. 30 ("[F]alling [interest] rates made it harder for investment managers to earn decent returns by purchasing relatively risk-free government or corporate bonds. Those pay less when rates fall.").

[45] TETT, FOOL'S GOLD at pp. 94–95. *See also* Morgenson, *How the Thundering Herd Faltered and Fell* ("This shift began in 2002, when low interest rates pushed investors to seek higher returns. 'Investors said, 'I don't want to be in equities anymore and I'm not getting any return in my bond positions,'' said William T. Winters, co-chief executive of JPMorgan's investment bank … 'Two things happened. They took more and more leverage, and they reached for riskier asset classes. Give me yield, give me leverage, give me return.' A few years ago, of course, some of the biggest returns were being harvested in the riskier reaches of the mortgage market. As C.D.O.'s and other forms of bundled mortgages were pooled nationwide, banks, investors and rating agencies all claimed that the risk of owning such packages was softened because of the broad diversity of loans in each pool.")

[46] *See* Gretchen Morgenson, *Behind Insurer's Crisis, Blind Eye to a Web of Risk*, N.Y. TIMES, Sep. 28, 2008, at A1 ("It is hard for us, without being flippant, to even see a scenario within any kind of realm of reason that would see us losing one dollar in any of those transactions.") (quoting Joseph J. Cassano, a former A.I.G. executive, August 2007)); Eric Dash and Julie Creswell, *Citigroup Saw No Red Flags Even as it Made Bolder Bets*, N.Y. TIMES, Nov. 23, 2008, at A1 ("The slice of mortgage-related securities held by Citigroup was 'viewed by the rating agencies to have an extremely low probability of default (less than .01 percent),' according to Citigroup slides used at the meeting [in the summer of 2007] and reviewed by the New York Times."); TETT, FOOL'S GOLD at pp. 44–45, 52–53.

these risks were offset by the advent of such protections as the geographic diversity of the loans securitized, the development of tranches with different levels of risk, and the ability of credit rating agencies to accurately identify potential risks of default.[47] At the same time, the increasing use of credit default swaps was perceived as a means of providing insurance against such potential defaults.[48]

Of course, the strongest incentive for investment in subprime mortgage-backed securities was the fact that, until approximately 2006, rising markets led to the perception that defaults were not a serious risk.[49] As noted by one investor: "In a rising market, even a bad loan is a good loan."[50]

At the same time, securitization created a perverse effect whereby those responsible for making the initial loans no longer had any financial risk in the event that the loans defaulted. That is to say, the process of securitization resulted in a system whereby the risk of not getting paid was transferred from the initial lenders to those who bought the mortgage-backed securities. The process has been described as follows:

> Before the advent of securitization, lenders typically handled loans from cradle to grave. They solicited loan applicants, underwrote and financed the mortgages, serviced the loans, and held the loans in portfolio to maturity. In turn, lenders largely made profits from the interest payments on the loans. Because lenders bore the full risk of default, they had strong incentives to turn down observationally risky borrowers. Securitization alters this incentive structure by unbundling the tasks in lending and parceling them out among a string of market actors. A mortgage broker may recruit loan applicants, a lender may

---

[47] *See* TETT, FOOL'S GOLD at pp. 44–56, 124, 276; Morgenson, *How the Thundering Herd Faltered and Fell* ("As C.D.O.'s and other forms of bundled mortgages were pooled nationwide, banks, investors and rating agencies all claimed that the risk of owning such packages was softened because of the broad diversity of loans in each pool."); *How Mortgages Became Part of the Mess*, WASH. POST, Dec. 16, 2008, <http://www.washingtonpost.com/wp-srv/business/interactives/frenzy/> (last accessed July 31, 2009).

[48] Steven Lohr, *In Modeling Risk, the Human Factor Was Left Out*, N.Y. TIMES, Nov. 5, 2008, at B1:

> Credit-default swaps … were originally created to insure blue-chip bond investors against the risk of default. In recent years, these swap contracts have been used to insure all manner of instruments, including pools of subprime mortgage securities. These swaps are contracts between two investors – typically banks, hedge funds and other institutions – and they are not traded on exchanges. The face value of the credit-default market has soared to an estimated $55 trillion. Credit-default swaps, though intended to spread risk, have magnified the financial crisis because the market is unregulated, obscure and brimming with counterparty risk (that is, the risk that one embattled bank or firm will not be able to meet its payment obligations, and that trading with it will seize up).

See also Morgenson, *Behind Insurer's Crisis, Blind Eye to a Web of Risk*; Robert O'Harrow, Jr. and Brady Dennis, *The Beautiful Machine*, WASH. POST, Dec. 29-31, 2008, at A01.

[49] TETT, FOOL'S GOLD at p. 123 ("Neither lenders nor borrowers worried much about the risk, because it was widely assumed that borrowers would simply refinance their loans at the end of their "teaser"-rate … Lenders also assumed that if borrowers did face problems meeting their mortgage payments, they could simply sell their properties, at a profit, and easily repay their loans."). *See also* Peter M. Zorn and Marsha J. Courchane, *Mortgage Market Players and Products* at p. 5 ("Delinquencies did not appear to be a serious problem in the early part of this decade, and as a consequence lenders appeared more concerned with market share and increasing originations than with the potential risk of default.").

[50] Ruth Simon and Michael Hudson, *Bad Loans Draw Bad Blood*, WALL ST. J., Oct. 9, 2006, at C1, *quoting* Nate Redleaf, research analyst, Imperial LLC.

> originate the loans, a specialist firm may provide the servicing, a trust may hold the loans, and outside investors may provide the financing.[51]

In separating the lending process from the risk of default, securitization created a system whereby the collection of fees, both by initial lenders as well as securitizers, became the main incentive to make a loan, as opposed to the creditworthiness of the borrowers.[52] In a June 2009 joint op-ed, Secretary of the Treasury Timothy Geithner and Director of the National Economic Council, Lawrence Summers, noted:

> In theory, securitization should serve to reduce credit risk by spreading it more widely. But by breaking the direct link between borrowers and lenders, securitization led to an erosion of lending standards, resulting in a market failure that fed the housing boom and deepened the housing bust.[53]

The types of practices resulting from this change in perspective were described in a newspaper article:

> WaMu [Washington Mutual] gave mortgage brokers handsome commissions for selling the riskiest loans, which carried higher fees, bolstering profits and ultimately the compensation of the bank's executives. WaMu pressured appraisers to provide inflated property values that made loans appear less risky, enabling Wall Street to bundle them more easily for sale to investors.
>
> ***
>
> For WaMu, variable-rate loans – option ARMs, in particular – were especially attractive because they carried higher fees than other loans, and allowed WaMu to book profits on interest payments that borrowers deferred. Because WaMu was selling many of its loans to investors, it did not worry about defaults: by the time loans went bad, they were often in other hands.[54]

In a rising market, there was no incentive to question the process. A lack of defaults made it appear that the process was properly balancing risks. Moreover, the process as a whole appeared to be benefiting all participants in the loan process.

---

[51] Strauss, *Turning a Blind Eye: Wall Street Finance of Predatory Lending*. *See also* Drew, *Frenzy*; Devin Leonard, *How Lehman Brothers Got Its Real Estate Fix*, N.Y. TIMES, May 3, 2009, at BU1; Day, *Villains in the Mortgage Mess?*

[52] *See* TETT, FOOL'S GOLD at p. 123 ("Back in the 1990s, when brokers made loans to subprime borrowers, they conducted checks to ensure that borrowers would be able to pay off their loans. However, during the boom, lenders had become a good deal less fussy about demanding that borrowers prove they had the income to repay loans.").

[53] Timothy Geithner and Lawrence Summers, *A New Financial Foundation*, WASH. POST, June 15, 2009. *See also* Dash and Creswell, *Citigroup Saw No Red Flags Even as it Made Bolder Bets* ("[Citigroup] pushed to get earnings, but in doing so, they took on more risk than they probably should have if they are going to be, in the end, a bank subject to regulatory controls… safe and soundness has to be no less important than growth and profits but that was subordinated by these guys." (quoting Roy Smith, a professor at the Stern School of Business at New York University)).

[54] Peter S. Goodman and Gretchen Morgenson, *Saying Yes, WaMu Built Empire on Shaky Loans*, N.Y. TIMES, Dec. 28, 2008, at A1; *See also* Mara der Hovanesian, *Sex, Lies, and Mortgage Deals*, BUS. WK., Nov. 24, 2008, at pp. 71–75.

> "All sides wanted to benefit. Lenders wanted large numbers of originations to grow their market share, borrowers wanted to stretch as far as they could to get into a house and build wealth. Investors wanted to make their best rate of return."[55]

In addition to the effects of securitization, arguments have also been made that the interest rate policies of the Federal Reserve created an environment that independently served both to weaken underwriting standards and to cause the steep increase in housing appreciation.[56]

The argument has been summarized as follows:

> [J]ust prior to the 2001 recession, the Federal Reserve began to cut interest rates to avert deflation and a deeper contraction of the economy. Soon after, home sales began to take off ahead of production. By 2003 these conditions helped create the tightest housing markets and the lowest interest rates in at least a generation.
>
> A dramatic run-up in home prices ensued as buyers with access to low-cost mortgage credit competed in bidding wars. For the first time since records were kept, median prices across the nation increased multiple times faster than incomes for several years in a row. The relaxation of underwriting requirements and the advent of mortgage products that initially reduced borrowers' payments – together with the unprecedented availability of mortgage speculators, investors, and home buyers with past credit problems – helped to fuel the boom.[57]

---

[55] Sarah Kellogg, *The Subprime Mortgage Meltdown: An Uncertain Future*, WASH. LAW., February 2008 (quoting Marsha Courchane, Vice President of CRA International. *See also* KINDLEBERGER, MANIAS, PANICS AND CRASHES: A HISTORY OF FINANCIAL CRISES, at p. 17 (1978) ("As firms or households see others making profits from speculative purchases and resales, they tend to follow. When the number of firms and households indulging in these practices grows large, bringing in segments of the population that are normally aloof from such ventures, speculation for profits leads away from normal, rational behavior to what had been described as "manias" or "bubbles." The word "mania" emphasizes the irrationality; "bubble" foreshadows the bursting.").

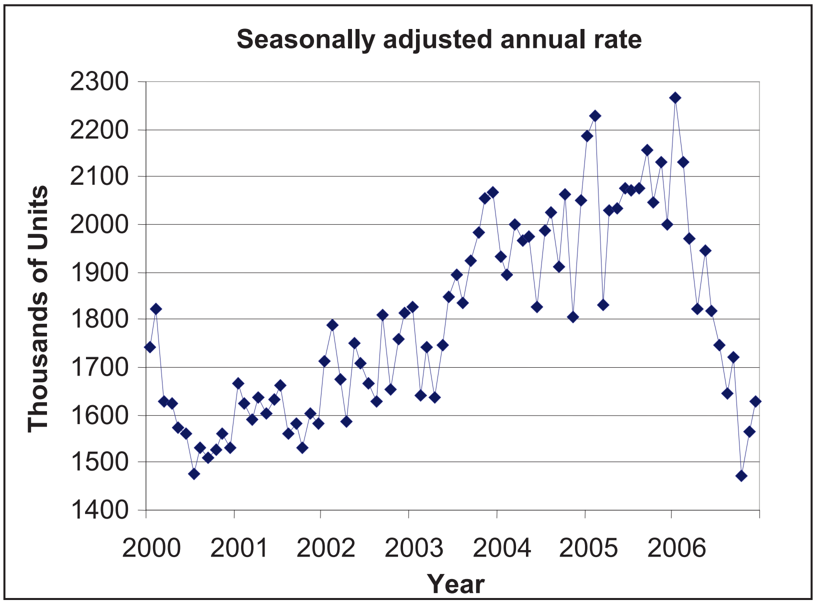
[56] *See* John B. Taylor, *How Government Created the Financial Crisis*, WALL ST. J., Feb. 9, 2009, at A19 ("Monetary excesses were the main cause of the boom. The Fed held its target interest rate, especially in 2003–2005, well below known monetary guidelines that say what good policy should be based on historical experience.").

Alan Greenspan, former chairman of the Federal Reserve, has contested this interpretation. *See* Alan Greenspan, *The Fed Didn't Cause the Housing Bubble*, WALL ST. J., Mar. 11, 2009, at A15 ("[The] decline in long-term interest rates across a wide spectrum of countries statistically explains, and is the most likely major cause of, real-estate capitalization rates that declined and converged across the globe, resulting in the global housing price bubble."). *See also Did the Fed Cause the Housing Bubble*, WALL ST. J., Mar. 27, 2009 (This opinion piece presents a variety of views on the topic); Roberts, *How Government Stoked the Mania*.

[57] JOINT CTR. FOR HOUS. STUDIES OF HARV. U., THE STATE OF THE NATION'S HOUSING 6 (2008). *See also* JOHN B. TAYLOR, GETTING OFF TRACK: HOW GOVERNMENT ACTIONS AND INTERVENTIONS CAUSED, PROLONGED, AND WORSENED THE FINANCIAL CRISIS 1–12 (2009) (Taylor argues that monetary excesses were the main cause of both the housing boom as well as the resulting bust. "In the United States such risk taking was encouraged by government programs designed to promote home ownership, a worthwhile goal but overdone in retrospect. During 2003-5, when short-term interest rates were still unusually low, the number of adjustable-rate mortgages (ARMs) rose to about one-third of total mortgages and remained at that high level for an unusually long time. This made borrowing attractive and brought more people into the housing markets, further bidding up housing prices. It is important to note, however, that the excessive risk taking and the low-interest monetary policy decisions are connected.").

The substance of this argument is reflected in Figures 2.1 and 2.2, below. As said Figures reflect, substantial correlation exists between the decrease in interest rates beginning in 2001 and the increase in the number of housing starts over the same period.[58]

Figure 2.1
New Privately-Owned Housing Units Started, 2000–2006



Note: Figures are based upon monthly housing starts, which the authors of the publication then seasonally adjust to an annual rate. Where the monthly reports show differences in the number of units because of revisions or other adjustments, the graphs above depict the more recently reported values.

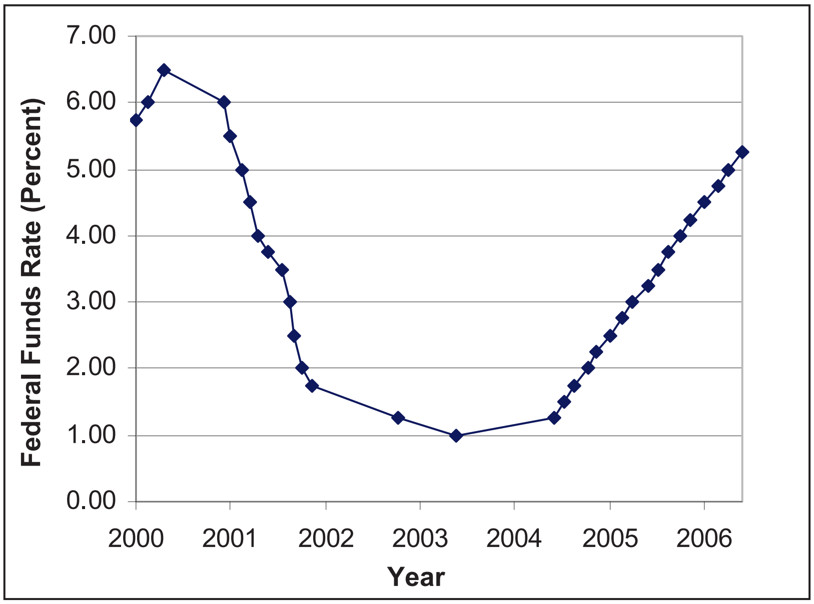
Source: Compiled by U.S. Commission on Civil Rights using the linked monthly reports (e.g., joint news release, U.S. Department of Commerce/U.S. Census Bureau and U.S. Department of Housing and Urban Development, New Residential Construction in June 2008, CB08-109, July 17, 2008, p. 4, table 3) for January 2001 through January 2009 from: U.S. Census Bureau, *New Residential Construction, Historic Press Releases*, June 16, 2009, <http://www.census.gov/const/www/newresconsthist.html> (last accessed Aug. 4, 2009).

Caption: The number of new privately-owned housing units started fluctuated each month. However it generally rose between mid-2000 and the beginning of 2006, and then fell during 2006. In particular, the number of such units started was 1,822,000 in February 2000 and 1,477,000 in July 2000. It rose to 2,228,000 in February 2005, fell to 1,833,000 in March 2005, and increased to 2,265,000 in January 2006. It dropped to 1,470,000, by November 2006, then recovered to 1,629,000 in December 2006.

---

[58] *See* SOWELL, THE HOUSING BOOM AND BUST at p. 7 ("In short, declining interest rates not only enable more people to be able to afford to buy a house, they enable the same person to buy a more expensive house without a higher monthly mortgage payment. In both cases, lower interest rates increase the demand for housing and thereby drive up home prices."). *See also* ElBoghdady and Cohen, *The Growing Foreclosure Crisis* ("The federal government played a central role in the boom. The Fed cut a key short-term rate to rev up the economy following the tech bust, enabling lenders to borrow money at low rates, lend that cash to home buyers at higher rates and then sell the mortgages to other institutions, said Esmael Adibi, an economist at Chapman University, south of Los Angeles.").

Figure 2.2
The Federal Funds Rate: The Interest Rate at Which Depository Institutions Lend Balances at the Federal Reserve to Other Depository Institutions Overnight, 2000–2006



Source: Compiled by U.S. Commission on Civil Rights using The Federal Reserve Board, *Monetary Policy, Open Market Operations*, Dec. 15, 2008, pp. 1–4, <http://www.federalreserve.gov/fomc/fundsrate.htm> (last accessed Aug. 4, 2009).

Caption: The federal funds rate, which is the overnight interest rate at which depository institutions lend money through the Federal Reserve to other depository institutions, was 5.75 percent in February 2000 and rose to 6.50 percent in May 2000. It remained as high as 6.00 percent in January 2001, but decreased steeply thereafter to 1.75 percent in December 2001, then to 1.25 percent in November 2002, and 1.00 percent in June 2003. It rose to 1.25 in June 2004, and more rapidly thereafter, reaching 5.25 percent in June 2006.

As the above figures reflect, as the interest rates established by the Federal Reserve declined, the demand for housing increased. That is to say, lower interest rates made monthly mortgage payments more affordable, thus increasing the demand for housing.[59] When these historically low interest rates were combined with federal policies seeking to increase homeownership, it is argued that all the prerequisites for a housing financial bubble were in place.[60]

---

[59] *See* KINDLEBERGER, MANIAS, PANICS AND CRASHES: A HISTORY OF FINANCIAL CRISES at p. 17. ("After a time, increased demand presses against the capacity to produce goods or the supply of existing financial assets. Prices increase, giving rise to new profit opportunities and attracting still further firms and investors. Positive feedback develops, as new investment leads to increases in income that stimulate further investment and further income increases. At this stage we may well get … "euphoria."); ALYSSA KATZ, OUR LOT: HOW REAL ESTATE CAME TO OWN US 110 (2009) ("Low interest rates were like a gift from the Federal Reserve to the homebuilding industry. Every percentage point that interest rates dropped was equivalent to another $8,000 or so off the price of the house.").

[60] It has been argued that these interest rate policies, combined with the search for greater returns, affected underwriting standards. *See* KATZ, OUR LOT: HOW REAL ESTATE CAME TO OWN US at p. 214:

> First the Fed lowered interest rates, in an effort to stimulate the economy after the dot-com bust and 9/11. The vastly increased potential for gain greased the securities-making machinery into gear, churning out thousands of new

> [T]he Federal Reserve decided to pursue an unusually expansionary monetary policy in order to counteract the downturn [in 2001]. When the Fed increased liquidity, money naturally flowed to the fastest expanding sector. Both the Clinton and Bush administrations aggressively pursued the goal of expanding homeownership, so credit standards eroded. Lenders and the investment banks that securitized mortgages used rising home prices to justify loans to buyers with limited assets and income. Rating agencies accepted the hypothesis of ever rising home values, gave large portions of each security issue an investment-grade rating, and investors gobbled them up.
>
> * * *
>
> By December 2001, the rate had been reduced to its lowest level since 1962. In 2002 the average Fed-funds rate was lower than in any year since the 1958 recession. In 2003 and 2004, the average Fed-fund rates were lower than in any year since 1955 when the rate series began.
>
> Monetary policy, mortgage finance, relaxed lending standards, and tax-free capital gains provided astonishing economic stimulus: mortgage loan originations increased an average of 56 percent per year for three years – from 1.05 trillion in 2000 to 3.95 trillion in 2003![61]

In an interview in May 2009, current Treasury Secretary Geithner acknowledged that interest rates had played a substantial role in the mortgage crisis. He noted, however, that many factors affect interest

---

> offerings. Investment bankers then faced a curious problem: more money seeking their high-yielding products, coming from all over the world, than they had raw material—mortgages—to sell. Their quest for new customers led to the astonishing deterioration of standards and suspension of rational judgment, in deciding who and what would qualify for the mortgages they were financing.

[61] Steven Gjerstad and Vernon L. Smith, *From Bubble to Depression?*, WALL ST. J., Apr. 6, 2009, at A15. *See also* LAWRENCE H. WHITE, CATO INST., HOW DID WE GET INTO THIS FINANCIAL MESS, briefing paper no. 110, Nov. 18, 2009, p. 1:

> The expansion in risky mortgages to underqualified borrowers was encouraged by the federal government. The growth of "creative" nonprime lending followed Congress's strengthening of the Community Reinvestment Act, the Federal Housing Administration's loosening of down-payment standards, and the Department of Housing and Urban Development's pressuring lenders to extend mortgages to borrowers who previously would not have qualified.
>
> Meanwhile, Freddie Mac and Fannie Mae grew to own or guarantee about half of the United States' $12 trillion mortgage market. Congressional leaders pointedly refused to moderate the moral hazard problem of implicit guarantees or otherwise rein in their hyperexpansion, instead pushing them to promote "affordable housing" through expanded purchases of nonprime loans to low-income applicants.
>
> The credit that fueled these risky mortgages was provided by the cheap money policy of the Federal Reserve. Following the 2001 recession, Fed chairman Alan Greenspan slashed the federal funds rate from 6.25 to 1.75 percent. It was reduced further in 2002 and 2003, reaching a record low of 1 percent in mid-2003 – where it stayed for a year. This set off what economist Steve Hanke called "the mother of all liquidity cycles and yet another massive demand bubble."
>
> The actual causes of our financial troubles were unusual monetary policy moves and novel federal regulatory interventions. These poorly chosen policies distorted interest rates and asset prices, diverted loanable funds into the wrong investments, and twisted normally robust financial institutions into unsustainable positions.

rates, and that the monetary environment is influenced not only by the Federal Reserve, but by global factors as well.

> Mr. Geithner: "But I would say there were three types of broad errors of policy and policy both here and around the world. One was that monetary policy around the world was too loose too long. And that created this just huge boom in asset prices, money chasing risk. People trying to get a higher return. That was just overwhelmingly powerful."
>
> Mr. Rose: "It was too easy."
>
> Mr. Geithner: "It was too easy, yes. In some ways less so here in the United States, but it was true globally. Real interest rates were very low for a long period of time."
>
> Mr. Rose: "Now, that's an observation. The mistake was that monetary policy by the Fed, was not …"
>
> Mr. Geithner: "Globally is what matters."
>
> Mr. Rose: "By central bankers around the world."
>
> Mr. Geithner: "Remember as the Fed started – the Fed started tightening earlier, but our long rates in the United States started to come down – even were coming down even as the Fed was tightening over that period of time, and partly because monetary policy around the world was too loose, and that kind of overwhelmed the efforts of the Fed to initially tighten. Now, but you know, we all bear a responsibility for that. I'm not trying to put it on the world."[62]

Strengthening this view is the fact that other areas of finance sensitive to the effects of low interest rates, but unaffected by U.S. government efforts to affirmatively further homeownership, also experienced increases in risky lending practices.[63] Two examples:

First, similar lending patterns existed with regard to domestic corporate debt.

> In the first six years of the decade, the business of repackaging *corporate* loans and derivatives had also boomed. In 2006 alone bankers sold $105.8 billion in CDOs [collateralized debt obligations] made out of risky corporate loans, double the previous

---

[62] *Geithner's Revelation*, WALL ST. J., May 12, 2009, at A16 (quoting *Charlie Rose: An Hour with Timothy Geithner, U.S. Treasury Secretary* (PBS television broadcast May 6, 2009) <http://www.charlierose.com/view/interview/10278> (last accessed July 17, 2009)).

[63] The historical relationship between cheap credit and speculation has been previously recognized. *See* KINDLEBERGER, MANIAS, PANICS AND CRASHES: A HISTORY OF FINANCIAL CRISES at p. 52 ("Speculative manias gather speed through expansion of money and credit or perhaps, in some cases, get started because of an initial expansion of money and credit.").

> year and seven times the volume at the start of the decade. They also sold $35.6 billion in CDOs built from corporate credit derivatives, ten times the amount sold in 2001.[64]

While corporate debt was equally subject to the pressures of securitization process and the decrease in interest rates, its fate cannot be related to policies governing affordable housing goals.

Second, other nations also experienced dramatic increases in home prices over the last decade, as well as the subsequent bust. In a recent report by the International Monetary Fund, countries such as the United Kingdom, Canada, and Australia were identified as experiencing similar housing appreciation and lending policies as the United States.[65] Other reports indicate that Ireland and Spain also have suffered through the same patterns.[66] In each case, while these nations were subject to global monetary conditions, and decreasing interest rates, they were not subject to U.S. housing incentives or affordable housing goals.

Nouriel Roubini, an economist from The Stern School of Business of New York University has noted:

> People talk about the American subprime problem, but there were housing bubbles in the U.K., in Spain, in Ireland, in Iceland, in a large part of emerging Europe, like the Baltics all the way to Hungary and the Balkans, "and most parts of the world." That's why the transmission and the effects have been so severe. It was not just the U.S. and not just 'subprime.' It was excesses that led to the risk of a tipping point in many different economies.[67]

These competing theories continue to foster vigorous debate about policies that may have caused the mortgage crisis. While the competing factors cannot be definitively resolved, they nonetheless provide a framework for analyzing the data contained in Chapter 3.

---

[64] TETT, FOOL'S GOLD at p. 147.

[65] *See* INTERNATIONAL MONETARY FUND, WORLD ECONOMIC OUTLOOK: HOUSING AND THE BUSINESS CYCLE (Apr. 2008).

[66] *See*, *e.g.*, *The Global Housing Boom: In Come the Waves*, ECONOMIST, June 16, 2005; Christopher Caldwell, *Ireland Shatters*, WKLY. STANDARD, May 11, 2009, at pp. 18–23; Timothy Egan–A New York Times Blog, *The Orphans of Ireland*, <http://egan.blogs.nytimes.com/2009/04/01/the-orphans-of-ireland/> (Apr. 1, 2009, 22:00 EST); Joe Thornhill, *The Property Pain in Spain*, DAILY MAIL, May 8, 2007, available at http://www.thisismoney.co.uk/mortgages-and-homes/homes-abroad/article.html?in_article_id=420094&in_page_id=505 (last accessed July 31, 2009); TAYLOR, GETTING OFF TRACK at pp. 7–11.

[67] James Fallows, *Dr. Doom Has Some Good News*, ATLANTIC, July–August 2009, at pp. 89–90.

CHAPTER 3: ANALYSIS OF THE EFFECTS OF FEDERAL POLICIES TO INCREASE MINORITY HOMEOWNERSHIP

I. Policies to Increase Minority and Low- and Moderate-Income Homeownership

In order to analyze the effects of government policies meant to increase minority homeownership, this section analyzes general data relating to homeownership and mortgage lending over the last 10 to 15 years. Where appropriate, the data attempts to determine the extent to which policies that sought to affirmatively further minority homeownership were effective. In addition, where practicable, the data sought to focus on the theories and critiques identified in the prior chapter.

A. Homeownership Patterns[1]

First examined is the homeownership rate generally, by race and ethnicity. This is followed by an examination of data relating to conventional loans made and denied, as well as an examination of denials measured against the applicants' credit history. Next, a similar examination is made with regard to refinanced loans. Finally, this section seeks to measure the recent growth in subprime loans as well as recent foreclosure statistics. As to the latter, data are examined with regard to the performance of fixed-rate and adjustable-rate mortgages, both in the prime and subprime markets.

B. Racial[2] *and Ethnic Disparities in Homeownership Over Time*

This section offers a review and analysis of racial and ethnic disparities in homeownership over time using data from a variety of sources including, but not limited to, the American Housing Survey,[3] the Decennial Census of Housing,[4] the Current Population Survey/Housing Vacancy Survey,[5] and the American Community Survey.[6]

While disagreement may exist as to its cause, there is no question that the rate of U.S. homeownership increased substantially over the last 15 years. In 1994, for example, the overall rate of U.S. homeownership was at 64 percent. At the peak of the real estate market, in 2004, this rate had increased to 69 percent, an increase of approximately 5 percentage points in only 10 years.

---

[1] *See* Figure 3.1, *infra*.

[2] Although the term "race" is used throughout, this report also examines data relating to ethnicity to the extent such information exists.

[3] Bureau of the Census, *American Housing Survey,* <http://www.2010census.biz/hhes/www/housing/ahs/ahs.html> (last accessed July 15, 2009).

[4] Bureau of the Census, *Census of Housing,* <http://www.census.gov/hhes/www/housing/census/histcensushsg.html> (last accessed July 15, 2009).

[5] Bureau of the Census, *Housing Vacancies and Homeownership*, <http://www.census.gov/hhes/www/housing/census/histcensushsg.html> (last accessed July 15, 2009).

[6] Bureau of the Census, *American Community Survey,* <http://www.census.gov/acs/www/index.html> (last accessed July 15, 2009).

As reflected in Figure 3.1, as of 1994, significant differences in homeownership rates[7] existed between Whites, American Indians/Alaskan Natives, Asians/Native Hawaiians/Pacific Islanders, Blacks, and Hispanics/Latinos.[8,9] White homeownership was at 67.7 percent in 1994. The next closest categories, American Indians and Asian/Pacific Islanders, had ownership rates approximately 16 percentage points lower than Whites, 51.7 percent and 51.3 percent respectively. Homeownership rates for Blacks and Hispanics/Latinos were even lower, reflecting ownership rates approximately 22 percentage points lower than Whites, with Black homeownership rates at 42.3 percent and Hispanic homeownership rates at 41.2 percent.

---

[7] The Current Population Survey/Housing Vacancies/Homeownership Survey is the source data on homeownership by race and ethnicity from 1994–2008. Bureau of the Census, Annual Statistics: 2008, *Housing Vacancies and Homeownership,* table 22, <http://www.census.gov/hhes/www/housing/hvs/annual08/ann08src.html> (last access Feb. 24, 2009).

Note that the U.S. Census Bureau states, "population controls that reflect the results of the 2000 decennial census are used in the CPS/HVS [Current Population Survey/Housing Vacancies and Homeownership Survey] estimation process for the first time in the first quarter 2003." Population controls that reflect the 1990 decennial census are used in the CPS/HVS from 1994 to 2002. Bureau of the Census, Annual Statistics: 2008, *Housing Vacancies and Homeownership,* appendix B, <http://www.census.gov/hhes/www/housing/hvs/annual08/ann08src.html> (last accessed Feb. 24, 2009).

The U.S. Census Bureau defines homeownership rate as the "proportion of households that are owners … It is computed by dividing the number of households that are owners by the total number of households." Bureau of the Census, Annual Statistics: 2008, *Housing Vacancies and Homeownership,* appendix A, <http://www.census.gov/hhes/www/housing/hvs/annual08/ann08def.html> (last accessed Feb. 24, 2009).

The Annual Statistics of the Current Population Survey/Housing Vacancy and Homeownership Survey provides two sets of data for 2002, one of which was revised. Commission staff sought clarification and was advised to use the revised data. Bob Callis, survey statistician, U.S. Census, telephone interview with Sock-Foon C. MacDougall, social scientist, U.S. Commission on Civil Rights, Jan. 5, 2009.

[8] For ease of reference, the above categories shall be shortened as follows: Whites, American Indians, Asians/Pacific Islanders, Blacks and Hispanics.

[9] The U.S. Census Bureau states, "The questions on race in the CPS are modified beginning in the first quarter 2003 to comply with the revised standards for federal statistical agencies. Respondents may now select more than one race. The Hispanic/Nonhispanic origin question continues to be asked separately." Bureau of the Census, Annual Statistics: 2007, *Housing Vacancies and Homeownership*, appendix B,

<http://www.census.gov/hhes/www/housing/hvs/annual07/ann07src.html> (last accessed Feb. 17, 2009).
The U.S. Census also states, "Race and Hispanics are two separate concepts in the federal statistical system. People who are Hispanics may be of any race. The overlap of race and Hispanic origin is the main comparability issue." Bureau of the Census, *Guidance on the Presentation and Comparison of Race and Hispanic Origin Data* <http://www.census.gov/population/www.socdemo/compraceho.html> (last accessed Mar. 2, 2009).

The Commission made the best possible equation of the racial categories of the 1990 and 2000 censuses in the following manner:

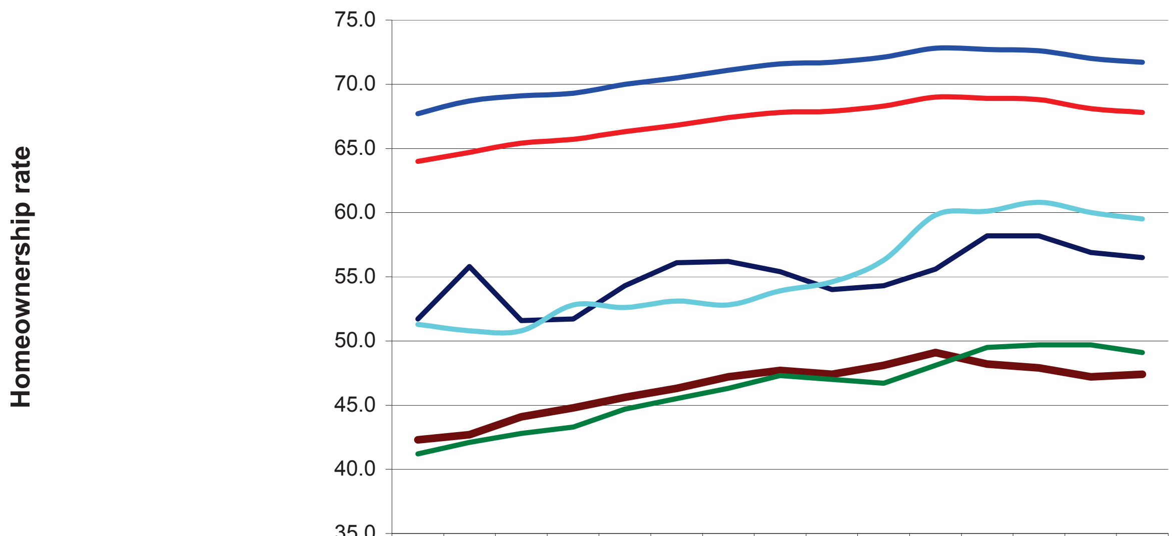
1990 census	2000 census	Best equivalence
White, total	White alone, total	White
American Indian or Alaskan Native	American Indian or Alaskan Native alone	American Indian or Alaskan Native
Asian or Native Hawaiian/Pacific Islander	Asian or Native Hawaiian/Pacific Islander alone	Asian or Native Hawaiian/Pacific Islander
Black, total	Black alone	Black

Note that homeownership rates from the Current Population Survey/Housing Vacancies/Homeownership Survey were tabulated by race and ethnicity for the first time in 1994. Bob Callis, survey statistician, the U.S. Census Bureau, telephone interview with Sock-Foon C. MacDougall, social scientist, U.S. Commission on Civil Rights, Jan. 5, 2009.

Over the following decade, ownership rates increased for each of these subgroups. Indeed, each minority racial and ethnic group showed stronger rates of growth than Whites. From 1994 through 2005, White homeownership increased from 67.7 percent to 72.7 percent, a gain of 5 percentage points. During the same period, however, homeownership rates increased 6.5 percentage points for American Indians, 8.8 percentage points for Asian/Pacific Islanders, 5.9 percentage points for Blacks, and 8.3 percentage points for Hispanics.

The homeownership differences among racial and ethnic groups, over time, are reflected in Figure 3.1.

Figure 3.1
Homeownership Rate by Race and Ethnicity, 1994–2008



	1994	1995	1996	1997	1998	1999	2000	2001	2002	2003	2004	2005	2006	2007	2008
U.S.	64.0	64.7	65.4	65.7	66.3	66.8	67.4	67.8	67.9	68.3	69.0	68.9	68.8	68.1	67.8
White	67.7	68.7	69.1	69.3	70.0	70.5	71.1	71.6	71.7	72.1	72.8	72.7	72.6	72.0	71.7
American Indian or Alaskan Native	51.7	55.8	51.6	51.7	54.3	56.1	56.2	55.4	54.0	54.3	55.6	58.2	58.2	56.9	56.5
Asian or Native Hawaiian/Pacific Islander	51.3	50.8	50.8	52.8	52.6	53.1	52.8	53.9	54.6	56.3	59.8	60.1	60.8	60.0	59.5
Black	42.3	42.7	44.1	44.8	45.6	46.3	47.2	47.7	47.4	48.1	49.1	48.2	47.9	47.2	47.4
Hispanic or Latino	41.2	42.1	42.8	43.3	44.7	45.5	46.3	47.3	47.0	46.7	48.1	49.5	49.7	49.7	49.1

Year

Note: 1. According to the U.S. Census, "population controls that reflect the results of the 2000 decennial census are used in the CPS/HVS [Current Population Survey/Housing Vacancies and Homeownership Survey] estimation process for the first time in the first quarter 2003." Population controls that reflect the 1990 decennial census are used in the CPS/HVS from 1994 to 2002. *See* Bureau of the Census, Annual Statistics: 2007, *Housing Vacancies and Homeownership*, appendix B, <http://www.census.gov/hhes/www/housing/hvs/annual08/ann08src.html> (last accessed Feb. 24, 2009).

2. The U.S. Census states that "The questions on race in the CPS are modified beginning in the first quarter 2003 to comply with the revised standards for federal statistical agencies. Respondents may now select more than one race. The Hispanic/Nonhispanic origin question continues to be asked separately. "*See* Bureau of the Census, Annual Statistics: 2007, *Housing Vacancies and Homeownership*, appendix B, <http://www.census.gov/hhes/www/housing/hvs/annual07/ann07src.html> (last accessed Feb. 17, 2009).

3. The U.S. Census also states that "Race and Hispanic are two separate concepts in the federal statistical system. People who are Hispanics may be of any race. The overlap of race and Hispanic origin is the main comparability issue." *See* Bureau of the Census, *Guidance on the Presentation and Comparison of Race and Hispanic Origin Data* <http://www.census.gov/population/www.socdemo/compraceho.html> (last accessed March 2, 2009),

The Commission made the best possible equation of the racial categories of the 1990 and 2000 censuses employed in Current Population Survey/Housing Vacancies/Homeownership Survey in the following manner:

1990 census racial categories employed for data from 1994-2002:	**2000 census racial categories employed for data from 2003-2008:**	**Described in this report as:**
White, total	White alone, total	White
American Indian or Alaskan Native	American Indian or Alaskan Native alone	American Indian or Alaskan Native
Asian or Native Hawaiian/Pacific Islander	Asian or Native Hawaiian/Pacific Islander alone	Asian or Native Hawaiian/Pacific Islander
Black, total	Black alone	Black

All of the above should be borne in mind.

4. The U.S. Census Bureau defines homeownership rate as the "proportion of households that are owners … It is computed by dividing the number of households that are owners by the total number of households." Bureau of the Census, Annual Statistics: 2008, *Housing Vacancies and Homeownership*, appendix A, < http://www.census.gov/hhes/www/housing/hvs/annual08/ann08def.html> (last accessed Feb. 24, 2009).

The Website for the Annual Statistics of the Current Population Survey/Housing Vacancy and Homeownership Survey posted two sets of data for 2002, one of which was marked revised. Bob Callis, survey statistician, U.S. Census, in a telephone interview with Sock-Foon C. MacDougall, social scientist, U.S Commission on Civil Rights, Jan. 5, 2009, stated that the revised data for 2002 should be used.

Source**:** Bureau of the Census, Annual Statistics: 2008, *The Current Population Survey/Housing Vacancies/Homeownership Survey*, table 22, <http://www.census.gov/hhes/www/housing/hvs/annual08/ann08ind.html> (last accessed July 21, 2009).

Caption: From 1995 to 2004, all groups experienced rising homeownership rates. The significant racial and ethnic disparities in homeownership rates evident in 1994 persisted though 2008 despite stronger rates of growth among minority groups.

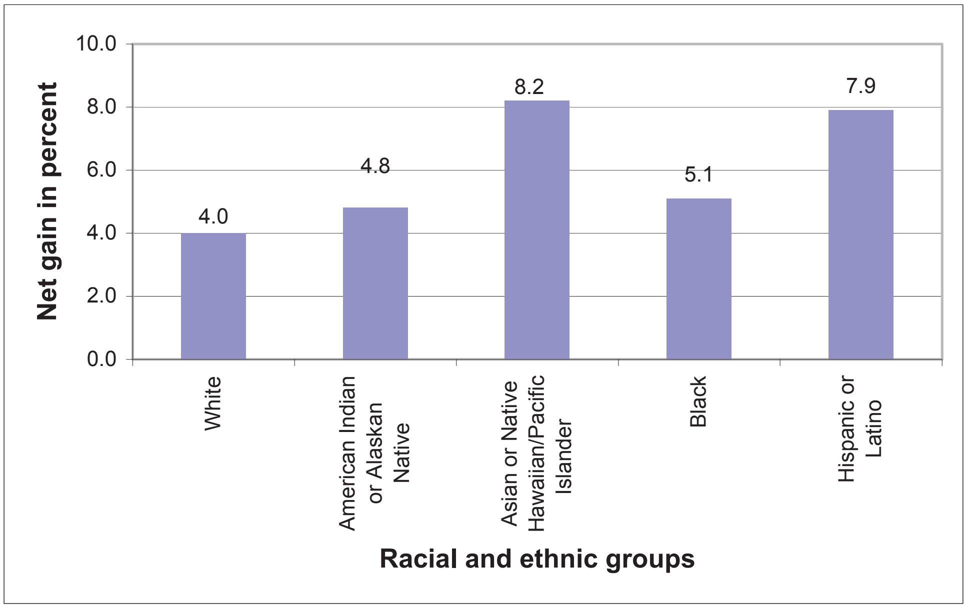
Even following the collapse of the housing bubble, racial and ethnic minority groups still showed stronger rates of growth than Whites. Through 2008, the net gain[10] in rates of homeownership indicates that Asians/Pacific Islanders' homeownership increased by 8.2 percentage points, Hispanics 7.9 percentage points, Blacks 5.1 percentage points and American Indians 4.8 percentage points. In each case, these groups exceeded the increase of White homeownership, which increased by 4 percentage points.

Figure 3.2 presents the differences in the rate of growth in homeownership among racial and ethnic groups.

---

[10] The net gain (more precisely, net change) is derived by adding the yearly homeownership rate gains and losses during this period. The result is positive for every racial/ethnic group, hence "net gain."

Figure 3.2
Net Gain in Homeownership Rate by Race and Ethnicity, 1994–2008



Note: The net gain for this period is derived by summing the yearly gains and losses in homeownership rate for each racial and ethnic group. The result in every case is a net gain. *See also* Table A.1 in Appendix A, "Change in Homeownership Rate by Race and Ethnicity," 1994–2008.

Source: Compiled by U.S. Commission on Civil Rights from the U.S. Census Bureau, Current Population Survey/Housing Vacancy Survey. *See* Bureau of the Census, Annual Statistics: 2008, *Housing Vacancy and Homeownership*, table 22, <http://www.census.gov/hhes/www/housing/hvs/annual08/ann08ind.html> (last accessed July 21, 2009).

Caption: During this period, the rate of growth in homeownership among racial and ethnic minorities was stronger than that of Whites, with Asians/Pacific Islanders and Hispanics showing highest gains

Despite the growth of minority homeownership, and the narrowing of the gap between the various groups, substantial racial and ethnic disparities in homeownership rates still remain. In 2008, the White homeownership rate stood at 71.7 percent, that of Asian/Pacific Islanders at 59.5 percent, American Indians at 56.5 percent, Hispanics at 49.1 percent, and Blacks at 47.4 percent. *See* Figure 3.1.

II. Review and Analysis of Mortgage Lending Statistics and Changes in Lending Standards

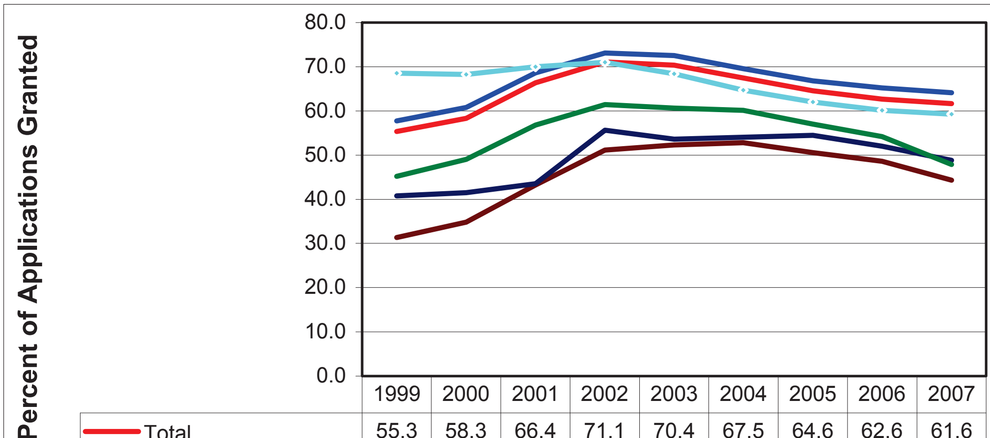
A. Disparities in Conventional Mortgage Loans by Race Over Time

Homeownership and mortgage lending are closely associated because the vast majority of home purchases are made with the help of a mortgage loan. An individual's inability to obtain a mortgage, for whatever reason, represents obstacles to owning one's own home.

The data provided in Figures 3.3 through 3.5 relate to conventional loans only. A conventional loan is an agreement that is not guaranteed or insured by the federal government under the Veterans Administration, the Federal Housing Administration, or the Rural Housing Service of the U.S. Department of Agriculture.

As reflected in Figure 3.3, conventional mortgage loans granted, as a percentage of conventional loan applications received, increased continuously for all racial and ethnic groups between 1999 and 2002. However, the degree of increase in the percentage of mortgage loans granted was not equally distributed among racial and ethnic groups. For example, the percentage of conventional loans made to Whites increased from 57.7 percent in 1999 to 69.6 percent in 2004, an increase of almost 12 percentage points. Even more dramatically, the percent of conventional loans made to Blacks increased from 31.4 percent in 1999 to 52.8 percent in 2004, an increase of 21.4 percentage points. Over the same period, Hispanics experienced approximately a 15 percentage point increase, while American Indians experienced a 13.4 percentage point increase. During the same period, Asians suffered a minor decrease of 3.9 percentage points. Figure 3.3 further shows that, although the percentage of conventional mortgage loans made to Blacks greatly increased between 1999 and 2004, Blacks were still far less likely than any other racial or ethnic group to receive such loans.

Figure 3.3
Conventional Loans Made to Applicants by Race and Ethnicity, 1999–2007



	1999	2000	2001	2002	2003	2004	2005	2006	2007
Total	55.3	58.3	66.4	71.1	70.4	67.5	64.6	62.6	61.6
White	57.7	60.8	68.6	73.1	72.6	69.6	66.8	65.2	64.1
Black	31.4	34.8	43.2	51.1	52.3	52.8	50.5	48.6	44.3
American Indian	40.7	41.5	43.5	55.6	53.6	54.1	54.4	52.0	48.8
Asian/Pacific Islander	68.6	68.2	70.0	71.0	68.4	64.7	62.0	60.1	59.2
Hispanic	45.2	49.0	56.8	61.4	60.6	60.2	57.0	54.2	47.9

Year

Note: Borrowers who fall into the “2 or more minority races,” “joint (white/minority race),” or “race not available” categories are excluded from this data. Note further that because of the manner in which HMDA data was collected, “Hispanics” are treated as a racial category in 1999 to 2003. In 2004 to 2007, “Hispanics” are an ethnicity, distinguished from non-Hispanics, hence their loans are also counted in the racial categories as “White,” “Black,” etc., where appropriate.

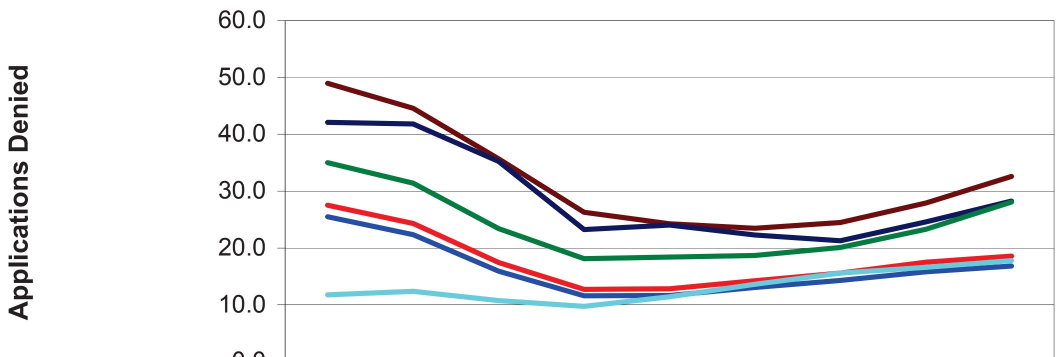
Source: HMDA Data, Table 4-2.

Caption: Between 1999 and 2002, conventional mortgage loans granted, as a percentage of conventional loan applications received, increased continuously for all racial and ethnic groups. Although the percentage of conventional loans made to Blacks continued to increase throughout 2004, they were still far less likely than any other racial or ethnic groups to receive such loans.

While minorities experienced the greatest percentage of growth as the market expanded, they also suffered the greatest decrease as the market began to tighten. From 2004 through 2007, conventional loans made to Whites decreased by 5.5 percentage points. Over the same period, however, the decrease for Blacks was 8.5 percentage points, and 12.3 percentage points for Hispanics. American Indians and Asian/Pacific Islanders suffered decreases of 5.3 percentage points and 5.5 percentage points, respectively.

Not surprisingly, as the percentage of conventional loans *granted* increased, the percentage of loan applications that were *denied* decreased. Figure 3.4 shows that, between 1999 and 2002, the percentage of conventional mortgage applications denied declined for all racial and ethnic groups.

Figure 3.4
Conventional Mortgage Applications Denied by Race and Ethnicity, 1999–2007



	1999	2000	2001	2002	2003	2004	2005	2006	2007
Total	27.5	24.3	17.5	12.7	12.8	14.2	15.6	17.5	18.6
White	25.5	22.3	15.9	11.6	11.6	13.1	14.3	15.8	16.8
Black	49.0	44.6	35.7	26.3	24.3	23.5	24.5	27.9	32.6
American Indian	42.1	41.8	35.3	23.3	24.0	22.3	21.3	24.6	28.3
Asian/Nat.Hawaiian	11.8	12.4	10.8	9.8	11.4	13.6	15.6	16.6	17.8
Hispanic	35.0	31.4	23.4	18.2	18.4	18.7	20.1	23.3	28.1

Year

Note: Borrowers who fall into the "2 or more minority races," "joint (white/minority race)," or "race not available" categories are excluded from this data. Note further that because of the manner in which HMDA data was collected, "Hispanics" are treated as a racial category in 1999 to 2003. In 2004 to 2007, "Hispanics" are an ethnicity, distinguished from non-Hispanics, hence their loans are also counted in the racial categories as "White," "Black," etc., where appropriate.

Source: HMDA Data, Table 4-2.

Caption: Between 1999 and 2007, Black borrowers consistently had the highest percentage of conventional mortgage loan applications denied. Between 2005 and 2007, Blacks, American Indians and Hispanics experienced the most dramatic increases in the percent of conventional mortgage applications denied.

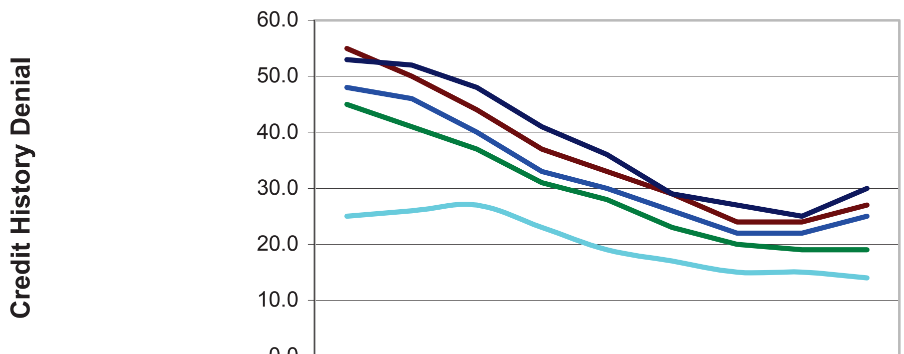
Interestingly, although the rate of conventional mortgage denials began increasing for most groups in 2004, denial rates for Blacks continued decreasing through 2004, going from 49 percent in 1999 to 23.5 percent in 2004, a decrease of 25.5 percentage points in only six years.

Between 2005 and 2007, however, the percent of conventional mortgage applications that were denied increased for all groups. The most dramatic increases were experienced by Blacks, American Indians[11] and Hispanics. According to Figure 3.4, the conventional mortgage denial rate increased over this period by 8 percentage points for both Blacks and Hispanics, but only by 2.5 percentage points for Whites.

As both Figures 3.3 and 3.4 indicate, there are discrepancies between racial and ethnic groups, both with regard to the rate by which conventional loans were approved, as well as the rate by which such loans were denied.

To examine possible explanations for this gap, Figure 3.5 details the denial of conventional mortgage loans based on credit history. An individual's credit history includes detailed information about that person's finances, including such things as late payments, bankruptcies, credit limits, balances, and actions taken to recover overdue debts.[12]

Figure 3.5
Denial of Conventional Mortgage Applications Based on Credit History by Race and Ethnicity, 1999–2007



	1999	2000	2001	2002	2003	2004	2005	2006	2007
White	48.0	46.0	40.0	33.0	30.0	26.0	22.0	22.0	25.0
Black	55.0	50.0	44.0	37.0	33.0	29.0	24.0	24.0	27.0
American Indian	53.0	52.0	48.0	41.0	36.0	29.0	27.0	25.0	30.0
Asian/Nat. Hawaiian	25.0	26.0	27.0	23.0	19.0	17.0	15.0	15.0	14.0
Hispanic	45.0	41.0	37.0	31.0	28.0	23.0	20.0	19.0	19.0

Year

[11] The Department of Treasury has pointed out that Native Americans face unique facts in the home mortgage market: "[f]inancing home mortgages … presents a major challenge, since most Indian Lands and Hawaiian Home Lands are held in trust by federal or state governments and cannot be sold or encumbered by a mortgage lien, except as authorized by the Secretary of the Interior or other appropriate state official." Community Development Financial Institutions Fund, Dept. of Treasury, *The Report of the Native American Lending Study*, 2001, p. 5. Practically, this "can effectively deprive Native Americans and Native Hawaiians of opportunities to use what is potentially the most valuable asset in their communities and thus creates and obvious barrier to the availability of debt financing." *Id*. at p. 31. For further information on unique lending concerns in Native communities, *see* FIRST NATIONS DEVELOPMENT INSTITUTE, BORROWING TROUBLE: PREDATORY LENDING IN NATIVE AMERICAN COMMUNITIES (2008).

[12] Applications for mortgage loans are, of course, denied for many reasons. These include the inability to verify the applicant's information, the applicant's debt-to-income ratio, as well as the applicant's credit history.

Note: Borrowers who fall into the “2 or more minority races,” “joint (white/minority race),” or “race not available” categories are excluded from this data. Note further that because of the manner in which HMDA data was collected, “Hispanics” are treated as a racial category in 1999 to 2003. In 2004 to 2007, “Hispanics” are an ethnicity, distinguished from non-Hispanics, hence their loans are also counted in the racial categories as “White,” “Black,” etc., where appropriate.

Source: HMDA Data, Table 8-2.

Caption: Between 1999 and 2005, the denial rates for mortgage loans based on credit history declined for Whites and Blacks and the gap between all racial and ethnic groups began to close. Between 2006 and 2007, the denial rates for mortgage loans based on credit history increased for Whites, Blacks and American Indians; remained unchanged for Hispanics; and decreased slightly for Asian/Native Hawaiians.

Figure 3.5 shows that the denial rates for mortgage loans based on credit history continuously declined between 1999 and 2005 for Whites and Blacks. At the same time, the gap between the various groups began to close. At the beginning of the time period in question, 1999, there was a gap of 7 percentage points between the denial rates of Whites (48 percent) and Blacks (55 percent) with similar credit histories. Over the next several years, the gap between these two races narrowed, decreasing to 4 percentage points by 2001, 3 percentage points by 2004, and 2 percentage points each year from 2005 to 2007.

Between 1999 and 2007, Asian/Pacific Islanders were the least likely to be denied a mortgage loan based on credit history. In 1999, only 25 percent of all mortgage application denials for Asian/Pacific Islanders were based on credit history. In comparison, 55 percent of all mortgage application denials for Blacks were because of credit history.

Between 2006 and 2007, as the market tightened, the numbers of those who were denied mortgage loans based on credit history increased by 3 percentage points for Whites and Blacks, and by 5 percentage points for American Indians. The percent of Hispanics and Asian/Pacific Islanders who were denied mortgages based on credit history either decreased slightly or remained unchanged.

B. Disparities in Refinance Loans by Race Over Time

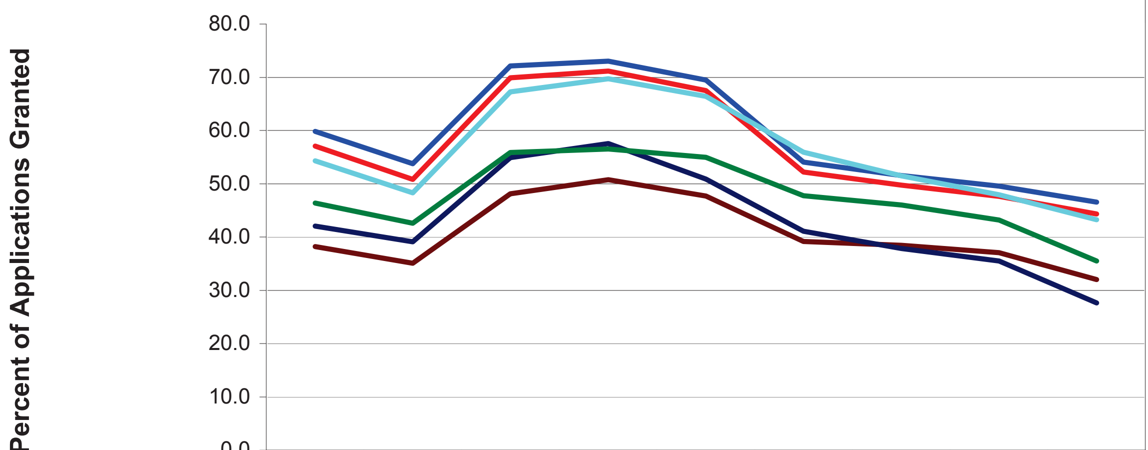
Home mortgage refinancing is a process by which a borrower pays off an existing loan with the proceeds from a new loan, using the same property as collateral. Borrowers seek refinancing in order to secure lower interest rates or to lower monthly mortgage payments. In addition, borrowers can use refinancing to tap into the equity in their homes, using the money for anything from home remodeling, to paying off high-interest rate bills, to incurring additional consumer debt.

Figures 3.6 through 3.8 portray the disparities that exist between racial and ethnic groups. Figure 3.6 examines the percentage of refinancing mortgage loans granted by race and ethnicity, while Figure 3.7 examines the percentage of loan applications denied by race and ethnicity. Figure 3.8 then shows the denial of refinance loan applications based on credit history.

Figure 3.6 shows that refinance loans granted, as a percentage of total refinance loan applications received, increased dramatically for all racial and ethnic groups during the peak years of the boom, between 2000 and 2002. For example, refinance loans made to the total population increased from 50.8 percent in 2000 to 71.2 percent in 2002, an increase of 20.4 percentage points over three years. Similar increases were experienced by all racial and ethnic groups. Whites experienced an increase of 19.3 percentage points, Blacks an increase of 15.7 percentage points, Hispanics an increase of 13.9

percentage points, Asian/Pacific Islanders an increase of 21.5 percentage points, and American Indians an increase of 18.5 percentage points—in each case, a striking increase in a period of only three years.

Figure 3.6
Refinance Loans Granted to Applicants by Race and Ethnicity, 1999–2007



	1999	2000	2001	2002	2003	2004	2005	2006	2007
Total	57.0	50.8	69.9	71.2	67.5	52.2	49.7	47.6	44.3
White	59.8	53.8	72.1	73.1	69.5	54.0	51.5	49.5	46.5
Black	38.2	35.1	48.1	50.8	47.7	39.1	38.4	37.1	32.0
American Indian	42.1	39.1	54.9	57.6	50.9	41.1	37.9	35.5	27.7
Asian/Pacific Islander	54.3	48.3	67.3	69.8	66.4	55.9	51.5	47.9	43.3
Hispanic	46.3	42.6	55.8	56.5	54.9	47.8	46.0	43.2	35.5

Year

Note: Borrowers who fall into the "2 or more minority races," "joint (white/minority race)," or "race not available" categories are excluded from this data. Note further that because of the manner in which HMDA data was collected, "Hispanics" are treated as a racial category in 1999 to 2003. In 2004 to 2007, "Hispanics" are an ethnicity, distinguished from non-Hispanics, hence their loans are also counted in the racial categories as "White," "Black," etc., where appropriate.

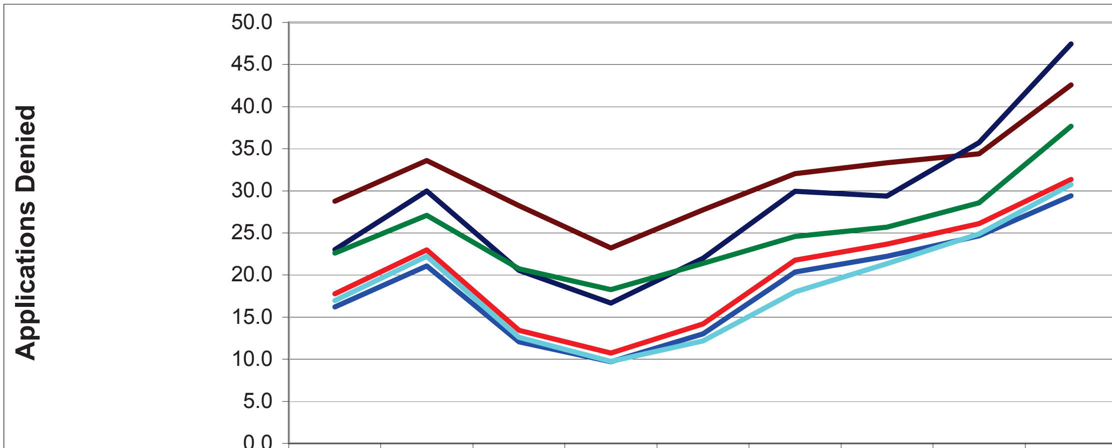
Source: HMDA Data, Table 4-3.

Caption: The percentage of refinance loans granted to all racial and ethnic groups, except Hispanics, increased by roughly 20 percent between 2000 and 2002. Between 2003 and 2007, the percentage of refinance loans granted continuously decreased for all racial and ethnic groups. By 2007, the percentages of loans granted were significantly lower than the percentage of loans granted in 1999.

Beginning in 2003, however, the percentage of refinance loans granted to all racial and ethnic groups began decreasing and continued in a downward spiral into 2007. For example, the percentage of refinance loans granted to Blacks decreased from 47.7 percent in 2003 to 32.0 percent in 2007. During this period, American Indians and Blacks continued to be less likely than other racial and ethnic minority groups to receive refinance loans.

As with the prior analysis of conventional loans,[13] the percentage of refinance loan applications granted was roughly the inverse of the percentage of refinance loans denied. Figure 3.7 shows that denial rates significantly decreased between 2000 and 2002 for all racial and ethnic groups. Blacks experienced the highest rate of denial of any racial or ethnic group, with the percentage of denials decreasing by 10.4 percentage points. During the same period, the rate of denials decreased by 11.4 percentage points for Whites, 8.8 percentage points for Hispanics, 12.5 percentage points for Asian/Pacific Islanders, and 13.3 percentage points for American Indians.

Figure 3.7
Refinance Loan Applications Denied by Race and Ethnicity, 1999–2007



	1999	2000	2001	2002	2003	2004	2005	2006	2007
Total	17.8	23.0	13.4	10.7	14.2	21.8	23.7	26.1	31.4
White	16.2	21.1	12.1	9.7	13.0	20.4	22.2	24.7	29.4
Black	28.8	33.6	28.2	23.2	27.8	32.0	33.3	34.4	42.6
American Indian	23.0	30.0	20.5	16.7	22.0	30.0	29.4	35.7	47.5
Asian/Native Hawaiian	17.0	22.2	12.6	9.7	12.2	18.0	21.4	24.9	30.8
Hispanic	22.6	27.1	20.7	18.3	21.4	24.6	25.7	28.6	37.7

Year

Note: Borrowers who fall into the "2 or more minority races," "joint (white/minority race)," or "race not available" categories are excluded from this data. Note further that because of the manner in which HMDA data was collected, "Hispanics" are treated as a racial category in 1999 to 2003. In 2004 to 2007, "Hispanics" are an ethnicity, distinguished from non-Hispanics, hence their loans are also counted in the racial categories as "White," "Black," etc., where appropriate.

Source: HMDA Data, Table 4-3.

Caption: Between 2000 and 2002, the percentage of refinance loan applications denied significantly decreased for all racial and ethnic groups. In 2003, the percentage of refinance loan applications denied continuously increased and by 2007, roughly 43 of refinance loans submitted by Blacks were denied and

[13] *See* Figures 3.3 through 3.5.

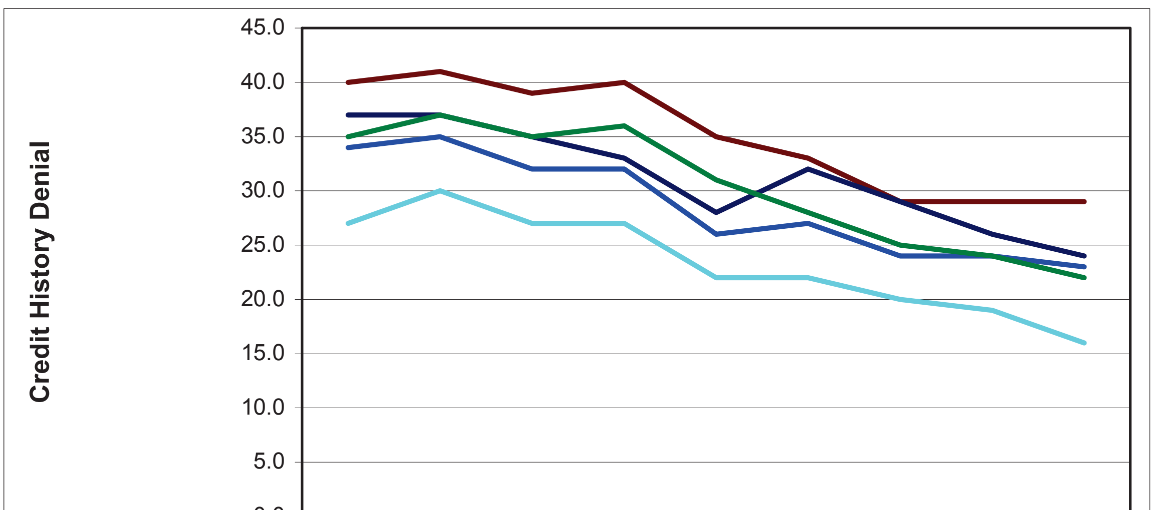
48 percent of refinance loans submitted by American Indians were denied. By 2007, the denial rates for refinance loans for all racial and ethnic groups were at the highest level since 1999.

Refinance denial rates increased steadily after 2002. By 2007, one-fourth or more of the total number of applications received for refinancing were denied regardless of race or ethnicity. Indeed, as of 2007, refinance loan denial rates were at their highest level than at any time during the previous eight years, with almost 43 percent of Black applicants being denied.

Applications for refinance loans are denied for the same reasons as mortgage loans, such as the inability to verify the applicant's information, the applicant's debt-to-income ratio, and the applicant's credit history. Figure 3.8 shows the denial of refinance loans based on credit history. As stated earlier, an individual's credit history includes a record of a person's past borrowing and repayment of debts, as well as detailed information about late payments, bankruptcies, credit limits, balances, and actions taken to recover overdue debts.

Figure 3.8 shows that, generally, denial rates for refinance loans as a result of credit history are higher than the denial rates for conventional mortgage loans.[14]

Figure 3.8
Denial of Refinance Loan Applications Based on Credit History by Race and Ethnicity, 1999–2007



	1999	2000	2001	2002	2003	2004	2005	2006	2007
White	34.0	35.0	32.0	32.0	26.0	27.0	24.0	24.0	23.0
Black	40.0	41.0	39.0	40.0	35.0	33.0	29.0	29.0	29.0
American Indian	37.0	37.0	35.0	33.0	28.0	32.0	29.0	26.0	24.0
Asian/Native Hawaiian	27.0	30.0	27.0	27.0	22.0	22.0	20.0	19.0	16.0
Hispanic	35.0	37.0	35.0	36.0	31.0	28.0	25.0	24.0	22.0

Year

[14] *See, e.g.,* Figure 3.5.

Note: Borrowers who fall into the “2 or more minority races,” “joint (white/minority race),” or “race not available” categories are excluded from this data. Note further that because of the manner in which HMDA data was collected, “Hispanics” are treated as a racial category in 1999 to 2003. In 2004 to 2007, “Hispanics” are an ethnicity, distinguished from non-Hispanics, hence their loans are also counted in the racial categories as “White,” “Black,” etc., where appropriate.

Source: HMDA Data, Table 8-3.

Caption: Between 2003 and 2007, refinance loan application denial rates based on credit history increased for all racial and ethnic groups, except American Indians. During this period, denial rates for Blacks were higher than for any other racial or ethnic group. Between 2003 and 2007, Asian/Native Hawaiians had the lowest denial rates.

The denial rates for refinance loans based on credit history continued to decline between 2002 and 2005; however, Blacks continued to have higher rates of denial than other racial and ethnic groups. While the denial rate for Blacks improved during this period, decreasing from 40.0 percent in 2002 to 29.0 percent in 2005, the comparable rates for Whites showed a decrease from 32.0 percent to 24.0 percent over the same period, while the respective decrease for Hispanics was from 36 percent to 25 percent.

Unlike the situation with conventional mortgages, the gap between the denial rates of Whites and Blacks regarding refinance loans did not close significantly over time. As discussed previously, the gap between Whites and Blacks relating to conventional loans closed from 7 percent in 1999 to 2 percent by 2005. The denial rate with regard to refinance loans, however, showed no such narrowing. There was a 6 percent gap between Whites and Blacks in 1999, and a 6 percent gap in 2007.

By 2007, the denial rates for refinance loans based on credit history were somewhat lower than those rates for conventional mortgage loans.

III. Prime and Subprime Lending

As discussed in Chapter 2, in the last decade and a half, lending practices relating to the home mortgage market have changed dramatically. A combination of improvements in technology, as well as the rise in securitization, drastically altered the nature and type of loans available to the public. The process has been described by experts at the Federal Reserve as follows:

> Traditionally, lenders offered consumers a relatively limited array of products at prices that varied according to the characteristics of the loan and property … not … the creditworthiness of the borrower. Effectively, borrowers either did or did not meet the underwriting criteria for a particular product, and those who met the criteria paid about the same price. …[15]

However, over time,

> improvements in information processing and the maturation of a robust secondary market for loans … spurred … among [other] changes … an evolution toward an explicitly risk-

---

[15] Robert B. Avery, Glenn B. Canner, and Robert E. Cook, Federal Reserve Board, *“New Information Reported under HMDA and Its Application in Fair Lending Enforcement,”* FED. RESERVE BULL., Summer 2005, at p. 349.

> based pricing of credit. Now the creditworthiness of individual borrowers can lead to different prices for the same product. Less-creditworthy applicants, or those either unwilling or unable to document their creditworthiness or income, are increasingly less likely to be turned down for a loan; rather, they are offered credit at higher prices.[16]

Loans in the higher-priced market, i.e., that cost more to the borrower, fall into either the "near prime" or "subprime" segment. Borrowers in the latter category pay the highest prices because they pose the greatest risk of default. Lower-price mortgages, i.e., those that cost less to the borrower, are referred to as the prime market.[17] These loans generally go to those who present less of a credit risk.

As significant pricing variability has emerged in the market, along with concerns about potential abuses in the subprime market, the Federal Reserve Board issued regulations requiring the disclosure of pricing in the higher-priced segment of the residential mortgage market. Its 2002 regulations require financial institutions to report the spread between the annual percentage rate (APR) on a loan and the rate on Treasury securities of comparable maturity for loans with spreads above designated thresholds. It then sought to select thresholds that would exclude the vast majority of prime rate loans while including the vast majority of subprime loans. For this purpose, it established a threshold of 3 percentage points of the spread for first liens and of 5 percentage points for second liens.[18]

Thus, HMDA data do "not identify subprime loans directly …. Rather, the HMDA data indicate which loans are categorized as 'higher priced,' including subprime loans and some alt-A loans."[19] Loans with no reported pricing data are "lower-priced" because the APR is below the threshold.

Given these standards, in the tables of this report, loans in HMDA data with no reported pricing data are designated as "prime" and those with reported pricing data in which the APR is above the threshold are designated as "subprime."

The subprime and prime distinctions in other data sources may reflect characteristics of the loan, such as characteristics of the loan or the borrower that reflect credit risk, rather than pricing. This is the case for the Mortgage Bankers Association's data on foreclosure and default rates used in this report. In collecting such data from banking firms, the Mortgage Bankers Association specifically instructs that they are to classify loans into prime and subprime "based on … internal or investor guidelines."[20] As explained elsewhere, "[t]he guidelines for what type of mortgage can be sold into a subprime pool vary across securitizers. In general, borrowers in subprime pools tend to have low credit scores and high loan-

---

[16] *Id*.

[17] *Id*.

[18] *Id.* at pp. 349-350.

[19] Randall Kroszner, "The Community Reinvestment Act and the Recent Mortgage Crisis," *The CRA: Perspectives on the Future of the Community Reinvestment Act,* A Joint Publication of the Federal Reserve Banks of Boston and San Francisco, February 2009, p. 9 n. 2.

[20] Mortgage Bankers Association, 3rd Quarter 2008 National Delinquency Survey of 1- to 4-unit, first-lien mortgage loans.

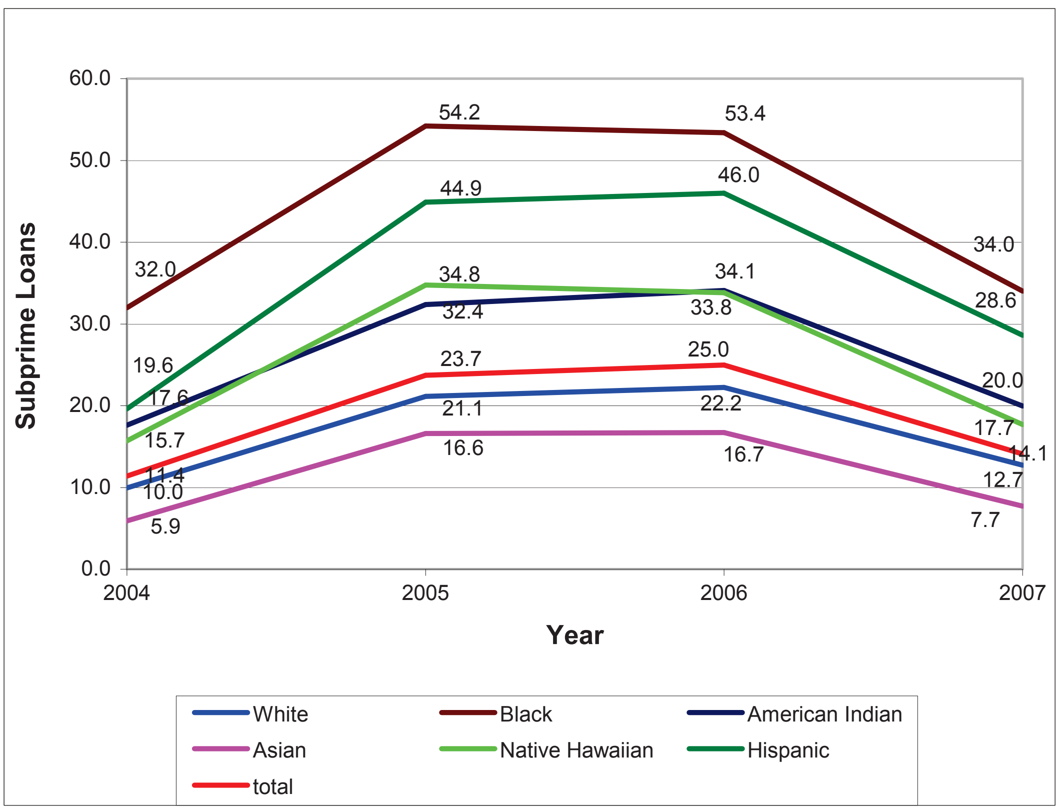
to-value ratios."[21] Thus, the distinction between higher- and lower-priced loans in HMDA data provides a good proxy, but not a direct measure, for prime versus subprime loans.

A. Prime vs. Subprime Lending by Race Over Time

Subprime mortgages were originally designed as loans to borrowers who did not qualify for conventional or conforming mortgage loans because they had less than perfect credit. These loans typically carry interest rates 3 to 5 percentage points higher than prime mortgages, as well as higher points and fees.[22]

As reflected in Figure 3.9, the percentage of subprime conventional mortgages given to all racial and ethnic groups increased dramatically between 2004 and 2005; remained high in 2006; and dramatically decreased between 2006 and 2007.

Figure 3.9
Subprime (Higher-Priced) Conventional Loans as a Percentage of Total Loans by Race and Ethnicity, 2004–2007



---

[21] *See* Andrew Haughwout, Christopher Mayer, and Joseph Tracy, Federal Reserve Bank of New York, *Subprime Mortgage Pricing: The Impact of Race, Ethnicity, and Gender on the Coast of Borrowing,* staff report no. 368, April 2009, p. 6.

[22] EDWARD M. GRAMLICH, SUBPRIME MORTGAGES: AMERICA'S LATEST BOOM AND BUST 17 (The Urban Institute Press 2007).

Note: Borrowers who fall into the "2 or more minority races," "joint (white/minority race)," or "race not available" categories are excluded from this data. Note further that because of the manner in which HMDA data was collected, "Hispanics" are treated as a racial category in 1999 to 2003. In 2004 to 2007, "Hispanics" are an ethnicity, distinguished from non-Hispanics, hence their loans are also counted in the racial categories as "White," "Black," etc., where appropriate.

Source: HMDA Table 11-3, 2004-2007. Data is for conventional home purchase loans, first lien, and does not include manufactured homes.

Caption: The percentage of higher-priced or subprime conventional loans granted as a percentage of total loans increased dramatically between 2004 and 2005 for all racial and ethnic groups. Between 2005 and 2006, the percentage of such loans given to all racial and ethnic groups showed no significant change. Between 2006 and 2007, although the percentage of higher-priced or subprime loans given to all racial and ethnic groups decreased significantly, Blacks were still far more likely than any other group to receive such loans.

For most minority groups, however, the percentage receiving such loans was higher than for Whites. For example, in 2004, nearly a third of all conventional mortgages given to Blacks were subprime loans. A year later, in 2005, that rate had increased dramatically to 54.2 percent. The rate for Hispanics in 2004 was 19.6 percent and 44.9 percent in 2005. During the same period, the figure for Whites was 10 percent in 2004 and 21.1 percent in 2005.

By 2007, the percent of subprime loans given to Blacks dropped to 34 percent. In 2007, for Black homeowners who had a subprime mortgage, the typical annual percentage rate was roughly 3 percentage points greater than the rate on a typical 30-year, fixed-rate conventional mortgage.[23]

As with subprime conventional loans, the percentage of Blacks who received subprime refinance loans was higher than for any other racial or ethnic group. As reflected in Figure 3.10, in 2005, 49.0 percent of all refinance loans granted to Blacks were subprime while more than half of all refinance loans to Blacks in 2006 were subprime. Over the same period, the figures for Hispanics were 33 percent in 2005 and 37.6 percent in 2006. The figures for Whites were 22.4 percent and 27.3 percent, respectively. Asian/Pacific Islanders were far less likely than any other racial group to receive subprime refinance loans. In 2005 only 15.2 percent of all refinance loans made to Asians were subprime.[24]

---

[23] RAKESH KOCHHAR, ANA GONZALEZ-BARRERA, AND DANIEL DOCKTERMAN, PEW HISPANIC CTR., THROUGH BOOM AND BUST: MINORITIES, IMMIGRANTS AND HOMEOWNERSHIP i (May 12, 2009).

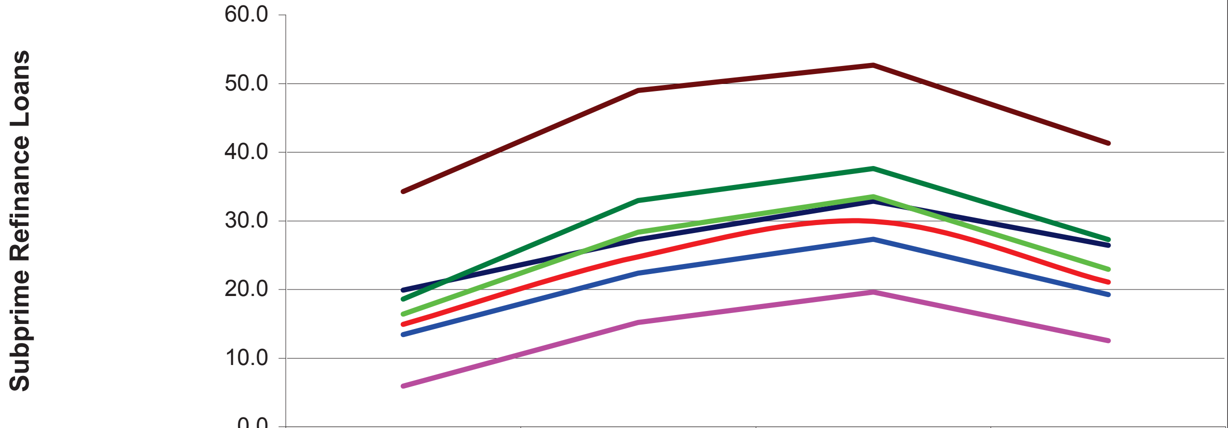
[24] The discrepancies in the rate at which different racial and ethnic groups have received subprime loans have been viewed by some as an indicium of predatory lending and/or discrimination. *See The Future of Fair Housing: Report of the National Commission on Fair Housing and Equal Opportunity*, Section V (December 2008); James H. Carr and David Berenbaum, Written Statement on behalf of the National Community Reinvestment Coalition to the U.S. Commission on Civil Rights, March 20, 2009; DEBBIE GRUENSTEIN BOCIAN, KEITH S. ERNST AND WEI LI, CTR. FOR RESPONSIBLE LENDING, UNFAIR LENDING: THE EFFECT OF RACE AND ETHNICITY ON THE PRICE OF SUBPRIME MORTGAGES (May 31, 2006).

Others, however, have contended that, when full creditworthiness is taken into account, the disparities between the various races and ethnicities shrink dramatically. As stated by one authority:

> [T]he central reality of the subprime mortgage market is that borrowers with higher incomes, greater wealth, and higher credit scores default less often than borrowers with lower incomes, less wealth, and lower credit scores. The unfortunate and troubling legacy of America's history of race relations is that, even in the 21st century, non-white borrowers as a group have lower incomes, less wealth, and lower credit scores on average than do white borrowers.

Brian P. Brooks, Written Statement to the U.S. Commission on Civil Rights, Mar. 20, 2009.

Figure 3.10
Subprime (Higher-Priced) Conventional Refinance Loans as a Percentage of Total Conventional Refinance Loans by Race and Ethnicity, 2004–2007



	2004	2005	2006	2007
Total	14.9	24.7	29.9	21.1
White	13.4	22.4	27.3	19.2
Black	34.3	49.0	52.7	41.3
American Indian	19.9	27.2	32.9	26.4
Asian	5.9	15.2	19.6	12.5
Native Hawaiian	16.4	28.4	33.5	22.9
Hispanic	18.6	33.0	37.6	27.3

Year

Note: Borrowers who fall into the "2 or more minority races," "joint (white/minority race)," or "race not available" categories are excluded from this data. Note further that because of the manner in which HMDA data was collected, "Hispanics" are treated as a racial category in 1999 to 2003. In 2004 to 2007, "Hispanics" are an ethnicity, distinguished from non-Hispanics, hence their loans are also counted in the racial categories as "White," "Black," etc., where appropriate.

Source: HMDA Data, Table 11-7.

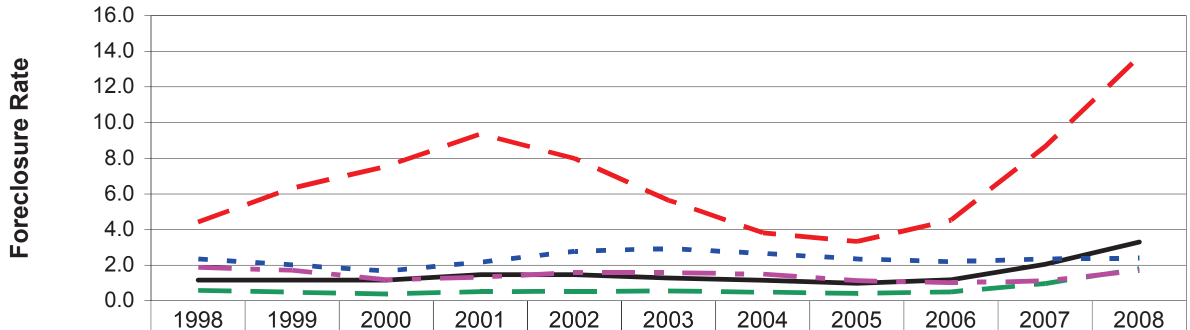
Caption: Between 2004 and 2006, the percentage of higher-priced or subprime conventional refinance loans granted as a percentage of total conventional refinance loans increased dramatically for all racial and ethnic groups. In 2006, more than 50 percent of all refinance loans granted to Blacks were higher-priced or subprime loans. All racial and ethnic groups were far less likely to receive such loans in 2007 than in earlier years.

By 2007, all racial and ethnic groups were far less likely to receive subprime refinance loans than in earlier years. For example, 26.4 percent of all refinance loans made to American Indians in 2007 were subprime, down from 32.9 percent in 2006. Although the percentage of Blacks receiving subprime loans decreased in 2007, they still received subprime loans at a significantly greater rate than other racial and ethnic groups.

IV. Foreclosure Rates by Type of Loan Over Time

An examination of foreclosure rates also reflects the significant difference between prime and subprime loans. Conventional subprime loans are significantly more likely than conventional prime, FHA or VA loans to enter foreclosure. Figure 3.11 shows that, during the late 1990s and early 2000s, foreclosure rates for subprime loans escalated, and peaked at 9.4 percent in 2001.

Figure 3.11
Mortgage Foreclosure Rates by Type of Loan, 1998–2008



	1998	1999	2000	2001	2002	2003	2004	2005	2006	2007	2008
All Loans	1.2	1.2	1.2	1.5	1.5	1.3	1.2	1.0	1.2	2.0	3.3
subprime	4.4	6.3	7.6	9.4	8.0	5.6	3.8	3.3	4.5	8.7	13.7
Prime	0.6	0.5	0.4	0.5	0.5	0.6	0.5	0.4	0.5	1.0	1.8
FHA	2.4	2.0	1.7	2.2	2.8	2.9	2.7	2.3	2.2	2.3	2.4
VA	1.9	1.7	1.2	1.3	1.6	1.6	1.5	1.1	1.0	1.1	1.7

Source: Mortgage Bankers Association, National Delinquency Survey.

Caption: Between 1998 and 2008, subprime loans had the highest foreclosure rates than prime, FHA or VA loans. Foreclosure rates began decreasing on subprime loans in 2002 and decreased continuously each year through 2005. By 2008, the foreclosure rate on subprime loans spiked to 13.7 percent. During this period, foreclosure rates for all other loans remained at 3 percent or less.

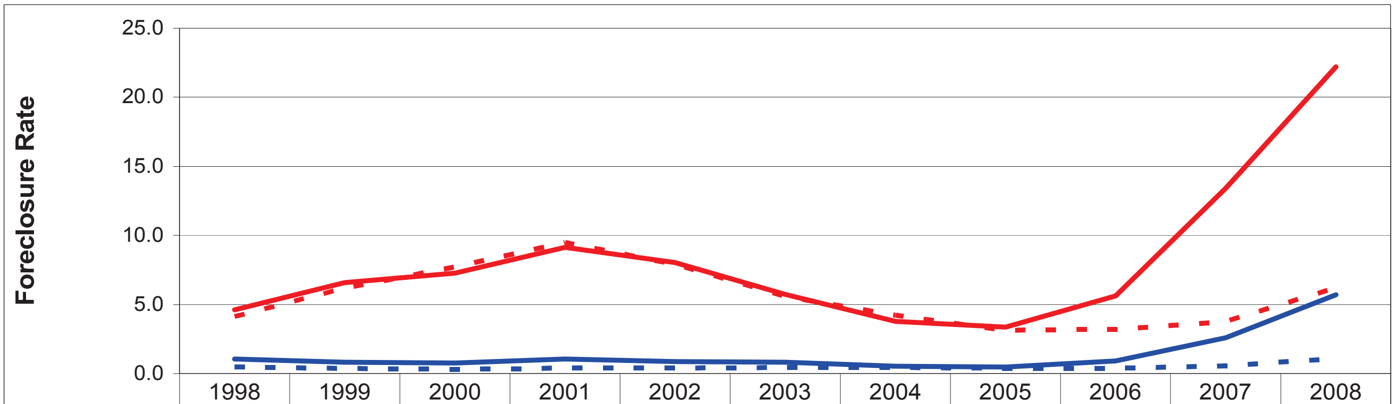
Not surprisingly, as overall homeownership rates crested in 2005,[25] overall foreclosure rates were at their lowest. As reflected in Figure 3.11, foreclosure rates for all types of loans began to increase in 2006. The increase in subprime loans was the most drastic. Specifically, foreclosure rates on conventional subprime loans went from 3.3 percent in 2005 to 8.7 percent in 2007 and were at 13.7 percent in 2008. Moreover, whereas the gap in foreclosure rates between subprime and prime loans had only been 2.9 percentage points in 2005, by 2008 the gap had increased to nearly 12 percentage points.

---

[25] *See* Figure 3.1.

Figure 3.12 depicts foreclosure rates for prime and subprime loans both for adjustable-rate mortgages (ARMs) and fixed-rate mortgages (FRMs). In an adjustable rate mortgage, the interest rate is generally fixed for a period of time, after which it will periodically adjust up or down based on some form of market index. In a fixed rate mortgage, the interest rate remains fixed for the term of the loan.

Figure 3.12
Conventional Foreclosure Rates by Type of Loan, 1998–2008



	1998	1999	2000	2001	2002	2003	2004	2005	2006	2007	2008
Subprime ARM	4.6	6.6	7.3	9.1	8.0	5.7	3.8	3.4	5.6	13.4	22.2
Subprime FRM	4.1	6.2	7.7	9.5	7.9	5.6	4.2	3.1	3.2	3.8	6.2
Prime ARM	1.1	0.8	0.8	1.1	0.9	0.8	0.5	0.5	0.9	2.6	5.7
Prime FRM	0.5	0.4	0.3	0.4	0.4	0.5	0.5	0.4	0.4	0.6	1.1

Source: Mortgage Bankers Association, National Delinquency Survey.

Caption: Between 1998 and 2005, foreclosure rates were highest for subprime loans, regardless of whether or not the loan was fixed or adjustable rate. After 2005, foreclosure rates on subprime adjustable rate loans began escalating and by 2008 those rates had increased from 5.6 to 22.2 percent. During this same period, foreclosure rates for subprime fixed rate mortgages also increased from 3.2 percent in 2006 to 6.2 percent in 2008. Prime adjustable rates mortgages also increased from 0.5 percent in 2005 to 5.7 percent in 2008.

While prime FRM foreclosure rates remained low throughout this period, subprime FRM loans were more volatile. Although the foreclosure rate for subprime FRMs had decreased to 3.1 percent by 2005, the percentage of foreclosures for these loans steadily increased, reaching a high of 6.2 percent in 2008.

Foreclosure rates for prime ARMs underwent greater change. Throughout much of the period examined, foreclosure rates for prime ARMs remained flat. Between 2006 and 2007, however, the rates nearly tripled from 0.9 percent to 2.6 percent. By 2008, the foreclosure rate for prime ARMs had increased to 5.7 percent.

By far the highest rate of foreclosure is attributable to subprime ARMs. While the rate of foreclosure for such loans declined from 2001 to 2005, it began to rise dramatically thereafter. By 2006, the rate of foreclosure for such loans had risen to 5.6 percent, and had increased to 13.4 percent by 2007. The rate of foreclosure in 2008 was 22.2 percent. By that point, the gap in foreclosure rates between prime ARMs and subprime ARMs, which had been at 2.9 percentage points in 2005, had increased to 16.5 percentage points.

V. Community Reinvestment Act

This section seeks to determine to what extent the requirements of the CRA may have affected residential mortgage lending practices and the existing mortgage crisis.

The mortgage lending data presented in this section are restricted to conventional first liens on home purchase and refinance loans for owner-occupied properties.[26] Conventional mortgage loans exclude those made by the Federal Housing Administration (FHA loans) and those guaranteed by the Veterans Administration (VA loans) and the Rural Housing Service of the U.S. Department of Agriculture (RHS Loan Programs).[27]

In order to analyze the effect of the CRA, this section examines practices of banking institutions and their affiliates and independent mortgage companies. This analysis compares and contrasts Performance with regard to a variety of factors in order to determine to what extent the CRA has played a role over approximately the last decade.

In this regard, section A compares the number and monetary value of (i) prime loans; (ii) subprime loans; and (iii) subprime loans by banking institutions and affiliates within their CRA assessment areas. Section B then examines the decreasing amount of mortgage lending within CRA assessment areas. Section C then examines the distribution of subprime loans from 2004 to 2007 by examining differences between loans made to low- and moderate-income individuals as compared to middle- and upper-income individuals. This section looks not only at loan counts and the monetary value of such loans, but the percent distributed by year and by lender type. Section D undertakes a similar analysis with regard to prime loans.

Sections E and F then analyze the race and types of neighborhoods that receive different types of loans. Section E examines mortgage lending by neighborhood income for the year 2006, while Section F examines mortgage lending by race for the same year.

---

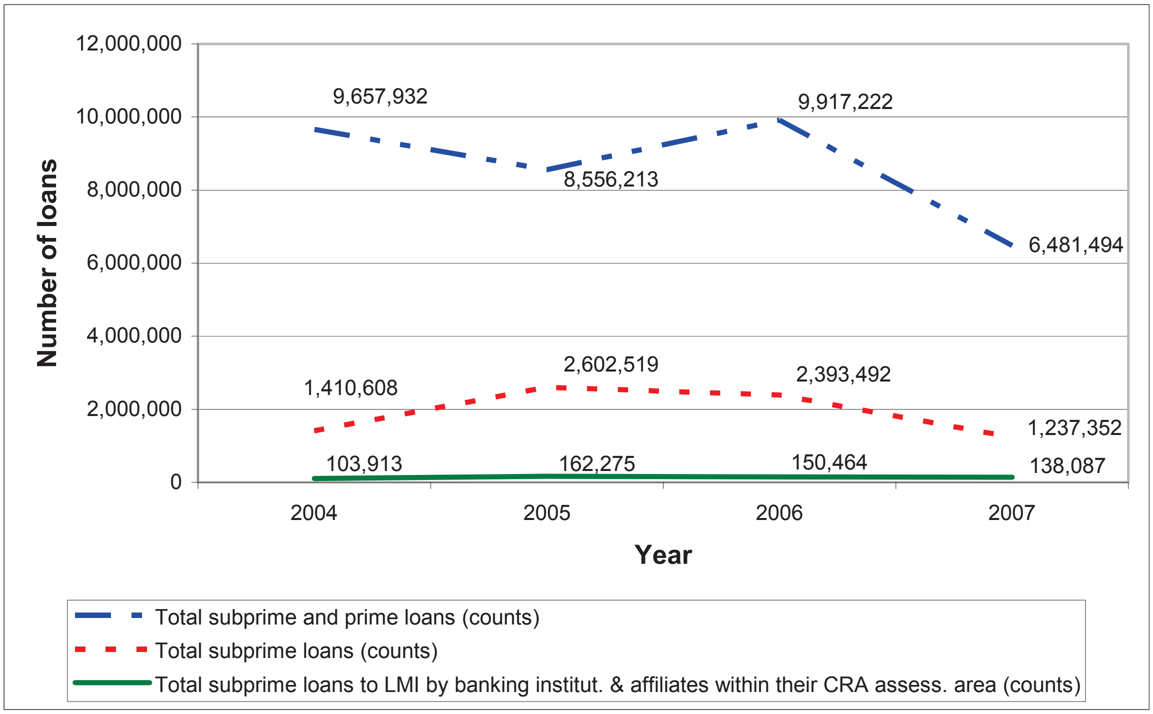
[26] Neighborhood income level in the context of the CRA is defined in relation to a designated geographic area's median family income; "lower income" is defined as less than 50 percent of the area's median family income; "moderate income," from 50 percent to less than 80 percent; "middle income," 80 percent to less than 120 percent; and "upper income," greater than or equal to 120 percent. Lower income neighborhoods include low- and moderate-incomes ones, the focus of the CRA. Non-lower income neighborhoods include middle and higher income ones. *See* The Federal Reserve, Briefing on CRA and Credit Scoring Issues to the U.S. Commission on Civil Rights, January 7, 2009 ("definition" and "the CRA"). Glenn B. Canner, senior advisor, The Federal Reserve, e-mail to Sock-Foon C. MacDougall, social scientist, U.S. Commission on Civil Rights, Apr. 29, 2009.

[27] Mortgage-X Mortgage Information Service, *Types of Mortgage Loans,* <http://mortgage-x.com/library.loans.htm> (last accessed Feb. 24, 2009).

A. Number and Monetary Value of Prime v. Subprime Loans

Figure 3.13 contrasts (i) the number of all loans (subprime and prime) originated, with (ii) all subprime loans originated, and (iii) all subprime loans originated by banking institutions and their affiliates within their CRA assessment areas to low- and moderate-income borrowers/neighborhoods.

Figure 3.13
Subprime (Higher-Priced) and All Home Mortgage Loans (Loan Counts) Originated, 2004–2007



Note: Restricted to conventional first liens on home purchase and refinance loans for owner-occupied properties.

Source: "Statistics on Mortgage Lending from HMDA Data," EXCEL spreadsheet, Glenn B. Canner, senior advisor, The Federal Reserve, to Sock-Foon C. MacDougall, social scientist, U.S. Commission on Civil Rights, Feb. 19, 2009.

Caption: During this period, the number of subprime loans compared to all loans originated was no more than 30.4 percent at its peak in 2005. At the same time, during its peak in 2007 the number of subprime loans made to low and moderate income borrowers/neighborhoods was no more than 11 percent of all such loans originated.

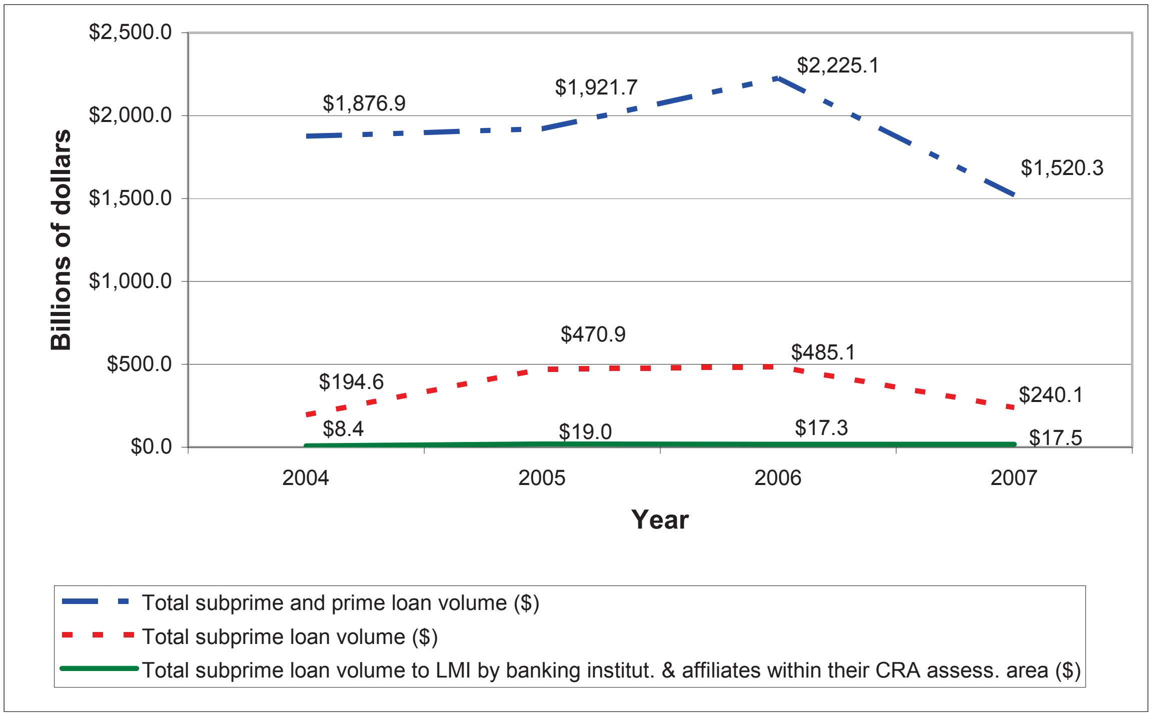
Figure 3.13 shows that, from 2004–2007, the total number of subprime loans made up just 14.6 percent of the total market in 2004, but that the number of such loans rose to 30.4 percent of the total market in 2005 as the market peaked. The share then fell to 24.1 percent in 2006, and by 2007 had decreased to 19.1 percent.[28]

[28] The figure for each year is obtained by calculating the percentage that the total number of subprime loans constituted of the total number of subprime and prime loans originated.

The total number of subprime loans that banking institutions and their affiliates made in their CRA assessment areas to low- and moderate-income borrowers/neighborhoods represented an even smaller fraction of the total number of subprime loans originated. Specifically, such loans constituted a mere 7 percent of all subprime loans in 2004, 6 percent in 2005 and 2006, and 11.0 percent in 2007.[29]

Figure 3.14 presents the same three categories, measured by the monetary value of the loans.

Figure 3.14
Subprime (Higher-Priced) and All Home Mortgage Loans (Billions of Dollars), 2004–2007



Note: Restricted to conventional first liens on home purchase and refinance loans for owner-occupied properties.

Source: "Statistics on Mortgage Lending from HMDA Data," EXCEL spreadsheet, Glenn B. Canner, senior advisor, The Federal Reserve, to Sock-Foon C. MacDougall, social scientist, U.S. Commission on Civil Rights, Feb. 19, 2009.

Caption: During this period, the monetary value of subprime loans compared to all loans originated was no more than 24.5 percent at its peak in 2005. Meanwhile, at its peak in 2007, the monetary value of subprime loans made to low and moderate income borrowers/neighborhoods was no more than 7 percent of all such loans originated.

---

[29] The figure for each year is obtained by calculating the percentage that the total number of subprime loans banking institutions and their affiliates originated to low- and moderate-income borrowers/neighborhoods within their CRA assessment areas constituted of the total number of subprime loans originated.

HMDA data show that the monetary value of subprime loans constituted 10.4 percent of overall volume in 2004, a percentage that climbed to 24.5 percent in 2005, decreased to 21.8 percent in 2006 and fell to 15.8 percent in 2007.[30]

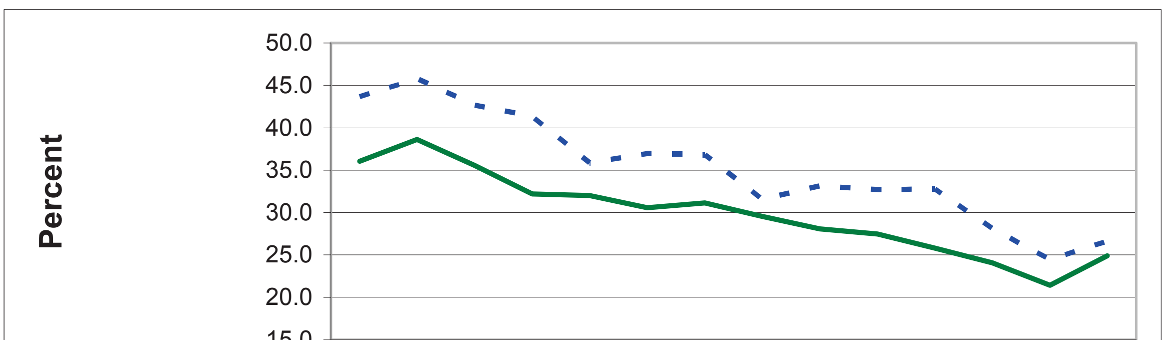
Most notably, the monetary volume of subprime loans made by banking institutions and their affiliates to lower-income borrowers/neighborhoods within their CRA assessment areas comprised a very small segment of all subprime loans originated. Specifically, such loans accounted for only 4 percent of overall volume from 2004 to 2006. By 2007, the figure had risen to only 7 percent.[31]

Based on Figures 3.13 and 3.14, the data indicate that, whether measured by number of loans, or monetary value of loans, subprime loans reached their peak in 2005 and never exceeded more than 30.4 percent of the number of loans or 24.5 percent of the value of loans. In addition, said data reflect that subprime loans made by banking institutions or their affiliates in their CRA assessment areas remained a marginal segment of the overall market.

B. Mortgage Lending Within CRA Assessment Areas 1993-2006

Figure 3.15 documents home purchase and refinance mortgage lending within CRA assessment areas, irrespective of neighborhood income.

Figure 3.15
Mortgage Lending Within CRA Assessment Areas, 1993–2006



	1993	1994	1995	1996	1997	1998	1999	2000	2001	2002	2003	2004	2005	2006
Home Purchase	36.0	38.6	35.5	32.2	32.0	30.6	31.1	29.6	28.1	27.5	25.8	24.1	21.4	24.9
Refinance	43.6	45.8	42.7	41.3	35.9	37.0	36.8	31.6	33.1	32.7	32.8	28.1	24.5	26.6

[30] The figure for each year is obtained by calculating the percentage that the total volume subprime loans constituted of the total volume of subprime and prime loans originated.

[31] The figure for each year is obtained by calculating the percentage that the total volume of subprime loans banking institutions and their affiliates originated to low- and moderate-income borrowers/neighborhoods within their CRA assessment areas constituted of the total volume of subprime loans originated.

Note: The Figure shows the percentage of mortgage loans originated by deposit-taking organizations within their assessment areas. This graph was presented by Ren S. Essene and William C. Apgar, "The 30th Anniversary of the CRA: Restructuring the CRA to Address the Mortgage Finance Revolution in *Revisiting the CRA: Perspectives on the Future of the Community Reinvestment Act,* A Joint Publication of the Federal Reserve Banks of Boston and San Francisco, February 2009, p. 22, exhibit 1: Assessment Area Lending Has Fallen Steadily. The source of the raw data for the graph is the JCHS enhanced HMDA database.

Source: Ren Essene, policy analyst, Federal Reserve Bank of Boston, PowerPoint file "Exhibit 1: Assessment Area Lending has Fallen" to Sock-Foon C. MacDougall, social scientist, U.S. Commission on Civil Rights, Mar. 25, 2009, 11.01 p.m.

Caption: Within CRA assessment areas, home mortgage lending and home refinancing particularly had been decreasing steadily from 1993 to 2006.

As reflected in Figure 3.15, mortgage lending within CRA assessment areas has decreased steadily over time. From 1993 to 2006, home purchase mortgage lending in CRA assessment areas, as a percent of all home purchase loans, decreased from 36.0 percent to 24.9 percent, a drop of 11.1 percentage points.[32]

In the same period, mortgage lending in CRA assessment areas for home refinancing decreased at a higher rate, falling from 43.6 percent to 26.6 percent, a drop of 17.0 percentage points. This decrease, at a time when overall mortgage lending was increasing, indicates that persons in lower-income neighborhoods were increasingly using banking institutions and their affiliates outside the CRA areas, as well as to independent mortgage companies.[33]

C. Distribution of Subprime Loans 2004-2007

Subprime loans traditionally have been made to those of low or moderate incomes. People of lower income often have lower levels of creditworthiness and, thus, are charged higher rates of interest on loans. The next set of Figures examines how such loans were distributed between low- and moderate-income borrowers/neighborhoods and middle- and upper-income borrowers/neighborhoods, for the period 2004-2007. Noticeably, as housing prices increased, even those with higher levels of income began obtaining subprime loans.

---

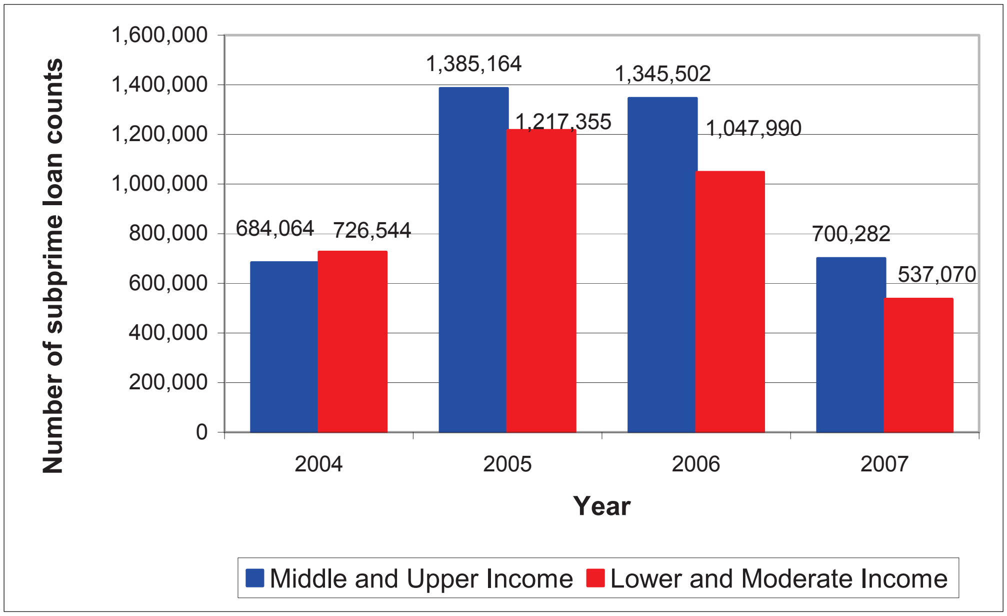
[32] *See* Ren S. Essene and William C. Apgar, "The 30th Anniversary of the CRA: Restructuring the CRA to Address the Mortgage Finance Revolution," *Revisiting the CRA: Perspectives on the Future of the Community Reinvestment Act*, A Joint Publication of the Federal Reserve Banks of Boston and San Francisco, February 2009, p. 22. *See also* KEVIN PARK, "SUBPRIME LENDING AND THE COMMUNITY REINVESTMENT ACT," JOINT CTR. FOR HOUSING STUDIES OF HARV. U.

[33] One possible explanation for this phenomenon was as follows:

> I don't want to say it's in the cultural DNA, but a lot of us who are older than 30 have some memory of disappointment or humiliation related to banks," Mr. Grannum said. "The white guy in the suit with the same income gets a loan and you don't?" "So you turn to local brokers, even if they don't offer the best rates." This may help explain an unusual phenomenon: Upper-income black borrowers in the region are more likely to hold subprime mortgages than even blacks with lower incomes, who often benefit from homeownership classes and lending assistance offered by government and nonprofits.

Michael Powell and Janet Roberts, *Minorities Affected Most as New York Foreclosures Rise*, N.Y. TIMES, May 16, 2009, at A1.

Figure 3.16
Distribution of Subprime (Higher-Priced) Mortgage Loans (Loan Counts) by Income of Borrowers and/or Neighborhood, 2004–2007



Note: Restricted to conventional first liens on home purchase and refinance loans for owner-occupied properties.

Source: "Statistics on Mortgage Lending from HMDA Data," EXCEL spreadsheet, Glenn B. Canner, senior advisor, The Federal Reserve, to Sock-Foon C. MacDougall, social scientist, U.S. Commission on Civil Rights, Feb. 19, 2009.

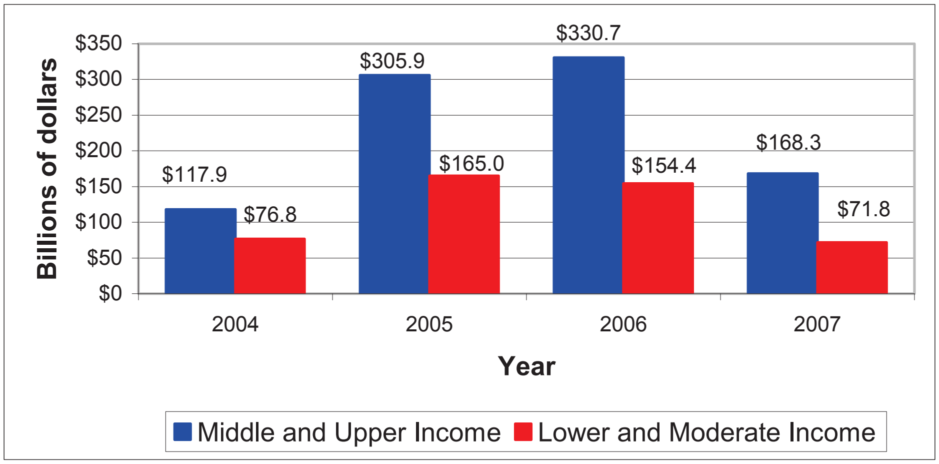
Caption: For three of the four years of this period, a smaller number of subprime loans were originated to low- and moderate-income borrowers/neighborhoods than to middle- and upper-income ones, with most being made in 2005.

Figure 3.16 shows that, except in 2004, the number of subprime loans made to low- and moderate-income borrowers/neighborhoods by financial institutions was smaller than that to middle- and upper-income ones. The number of such loans to low and moderate borrowers was among the highest in 2005 and 2006 and evidenced considerable variation over time. Rising from about 726,000 in 2004, such loans peaked at 1.2 million in 2005, an increase of 67.6 percent. In 2006, the number of such loans decreased somewhat, by 13.9 percentage points, but remained above a million. By 2007, they had fallen precipitously, bottoming out at about 537,000, a decrease of 48.8 percentage points over the previous year.

For every year, other than 2004, the number of middle- and upper-income subprime loans exceeded those for low- and moderate-income groups.

Figure 3.17 shows the distribution of subprime loans broken down by volume.

Figure 3.17
Distribution of Subprime (Higher-Priced) Mortgage Loan Volume (Billions of Dollars) by Income of Borrowers and/or Neighborhood Income, 2004–2007



Note: Restricted to conventional first liens on home purchase and refinance loans for owner-occupied properties.

Source: The Reserve Board, "Statistics on Mortgage Lending from HMDA Data," EXCEL spreadsheet, Glenn B. Canner, senior advisor, to Sock-Foon C. MacDougall, social scientist, U.S. Commission on Civil Rights, Feb. 19, 2009.

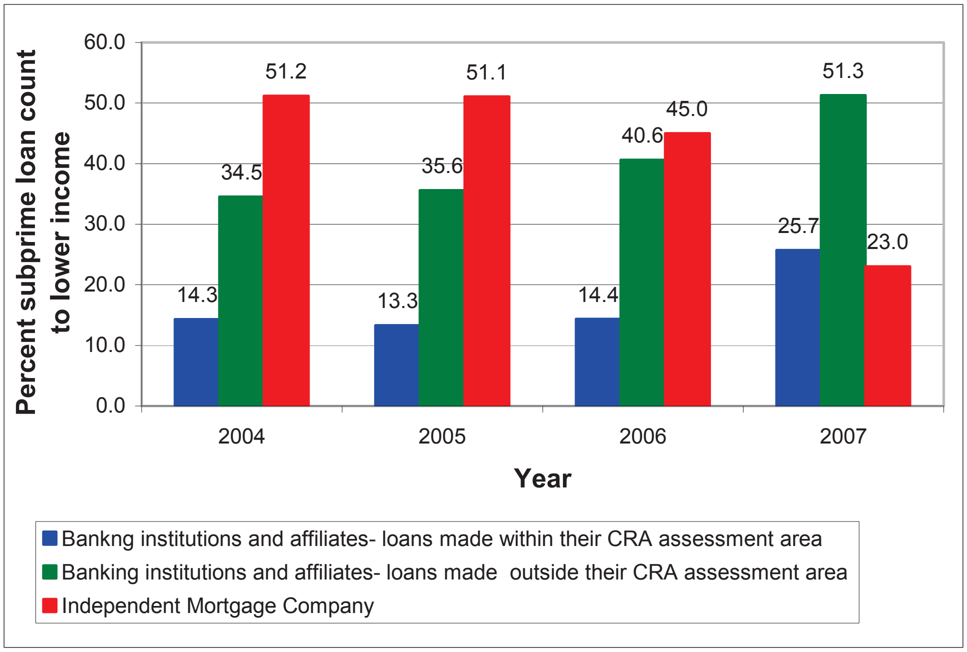
Caption: The monetary value of subprime loans to low- and moderate-income borrowers/neighborhoods is consistently lower than that to middle- and upper-ones and evidenced decline. Meanwhile, the overall monetary value of subprime loans had grown substantially since 2004, noticeably in 2005 and 2006.

Figure 3.17 reflects that, during this period, the monetary volume of subprime loans to middle- and upper-income borrowers/neighborhoods consistently exceeded those made to lower- and moderate-income groups. Indeed, during the critical years of 2005, 2006, and 2007, subprime loans to lower- and moderate-income borrowers/neighborhoods were often less than half the dollar value of subprime loans made to middle- and upper-income borrowers/neighborhoods.

In addition, Figure 3.17 reflects the growth of subprime loans generally over this period. For example, the total value of subprime loans reflected in Figure 3.17 for 2004 was 194.7 billion. By 2005 that figure had risen to 470.9 billion, and by 2006 the figure had reached 485.1 billion.

The next set of Figures seeks to examine to what extent subprime loans were made within CRA assessment areas. For that purpose, Figure 3.18 presents the number of subprime loans originated by different lender types, including independent mortgage companies.

Figure 3.18
Percent Distribution of Subprime (Higher-Priced) Mortgage Loans (Loan Counts) to Lower-Income of Borrowers and/or Neighborhoods by Lender Type, 2004–2007



Note: Restricted to conventional first liens on home purchase and refinance loans for owner-occupied properties.

Source: "Statistics on Mortgage Lending from HMDA Data," EXCEL spreadsheet, Glenn B. Canner, senior advisor, The Federal Reserve, to Sock-Foon C. MacDougall, social scientist, U.S. Commission on Civil Rights, Feb. 19, 2009.

Caption: Independent mortgage companies dominated the market for subprime loans to low and moderate borrowers/neighborhoods from 2004 through 2006. Banking institutions and their affiliates made the smallest percentage of subprime loans within their assessment areas but growth of such loans outside these areas was discernable, particularly in 2006 and 2007.

As reflected above, independent mortgage companies made the highest percentage of such loans for three of the four years, with their market share falling precipitously in 2007.[34] In the first two years, they consistently claimed a majority of subprime loans. By 2006, however, that share had decreased to 45 percent and, by 2007, their market share fell further to 23.0 percent.

Of the subprime loans made by banking institutions and their affiliates, the smallest percentages were originated within an institution's CRA assessment area. From 2004 to 2006, for example, the figures were consistently low, 14.3, 13.3, and 14.4 percent, respectively. Only in 2007 did this share in the market increase rising to 25.7 percent.

---

[34] The rather dramatic increase and decrease in market shares in 2007 on the part of the banking institutions and their affiliates and the independent mortgages, respectively, might be explained by a reduction in the number of lenders. In 2007, 169 lenders that reported data for 2006 ceased operations and did not report in 2007. With the exception of two lenders, all were independent mortgage companies. The Federal Reserve, Briefing on the 2007 HMDA Data to the U.S. Commission on Civil Rights, Jan. 28, 2009.

At the same time, progressively higher percentages were originated outside CRA assessment areas. Such loans initially increased modestly, rising from 34.5 percent in 2004 to 35.6 percent in 2005. They then increased to 40.6 in 2006, and finally to 51.3 percent in 2007. Between 2004 and 2007, there was an increase of 16.8 percentage points.

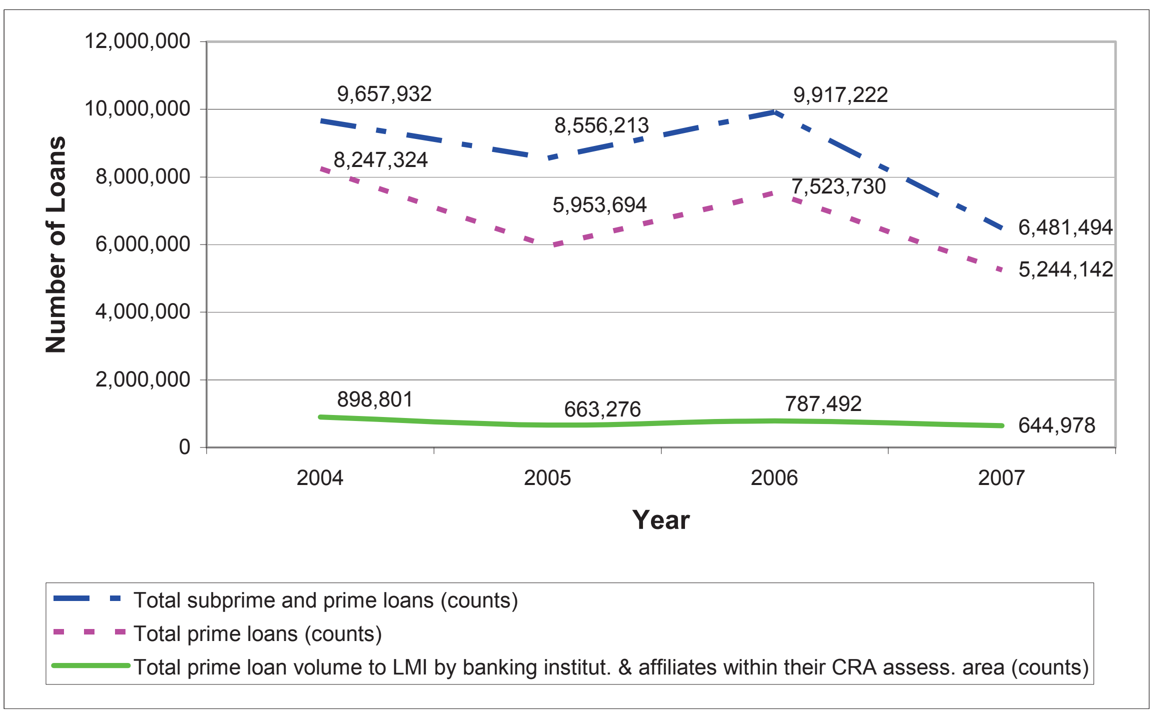
Based on Figures 3.16-3.18, two major points can be discerned. First, during the time period in question, middle- and upper-income borrowers/neighborhoods were the largest consumers of subprime loans. This is so whether measured by number of loans or monetary volume. Second, as reflected in Figure 3.18, the largest percent of subprime loans, by a substantial margin, was made by either independent mortgage companies or banking institutions outside their CRA assessment areas.

Both of these findings call into question not only the argument that the CRA played a major role in the current mortgage crisis, but also the CRA's continued relevance as a means to ensure sound lending to low- and moderate-income borrowers/neighborhoods.

D. Distribution of Prime Loans 2004-2007

The focus of the next examination is on the extent of prime loans originated within CRA assessment areas. To that end, Figure 3.19 examines the number of such loans, while Figure 3.20 examines their monetary value.

Figure 3.19
Distribution of Prime (Lower-Priced) and All Home Mortgage Loans (Loan Counts) Originated, 2004–2007



Note: Restricted to conventional first liens on home purchase and refinance loans for owner-occupied properties.

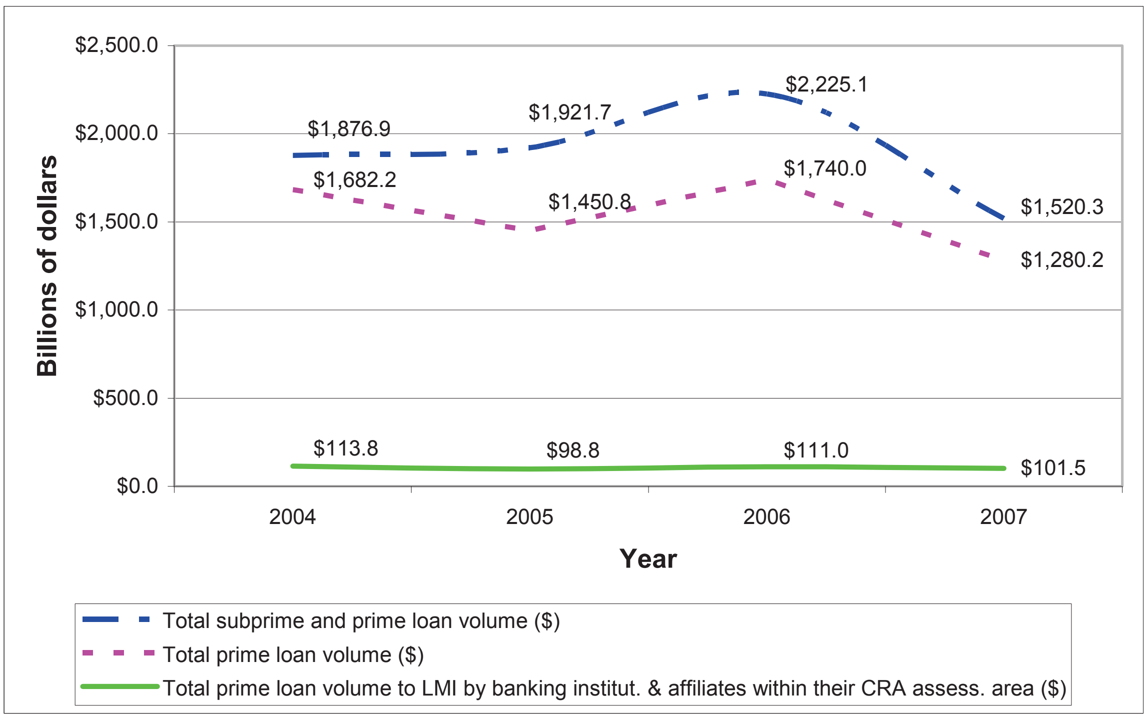
Source: "Statistics on Mortgage Lending from HMDA Data," EXCEL spreadsheet, Glenn B. Canner, The Federal Reserve, senior advisor, to Sock-Foon C. MacDougall, social scientist, U.S. Commission on Civil Rights, Feb. 19, 2009.

Caption: During this period, prime loans constituted a substantial percentage of all loans originated, no less than 69.6 percent in 2005. In contrast, at its peak in 2007 prime loans to low- and moderate-income borrowers/neighborhoods comprised no more than 12 percent of all prime loans originated.

As reflected in Figure 3.19, the total number of prime loans constituted a substantial proportion of all loans originated (prime and subprime), particularly in 2004 and 2007. In percentage terms, prime loans constituted 85.4 percent of the total in 2004, 69.6 percent in 2005, 75.9 percent in 2006, and 80.9 percent in 2007.[35]

At the same time, the number of prime loans that banking institutions and their affiliates originated to low- and moderate-income borrowers/neighborhoods within their CRA assessment areas was consistently a very small portion of all prime loans originated. In percentage terms, such loans represented only 11 percent of the total in 2004 and 2005, 10 percent in 2006, and 12 percent in 2007.[36]

Figure 3.20
Distribution of Prime (Lower-Priced) and All Home Mortgage Loans (Billions of Dollars), 2004–2007



Note: Restricted to conventional first liens on home purchase and refinance loans for owner-occupied properties.

Source: "Statistics on Mortgage Lending from HMDA Data," EXCEL spreadsheet, Glenn B. Canner, senior advisor, The Federal Reserve, to Sock-Foon C. MacDougall, social scientist, U.S. Commission on Civil Rights, Feb. 19, 2009.

---

[35] The figure for each year is obtained by calculating the percentage that the total number of prime loans constituted of the total number of subprime and prime loans originated.

[36] The figure for each year is obtained by calculating the percentage that the total number of prime loans banking institutions and their affiliates originated to low- and moderate-income borrowers/neighborhoods within their CRA assessment areas constituted of the total number of prime loans originated.

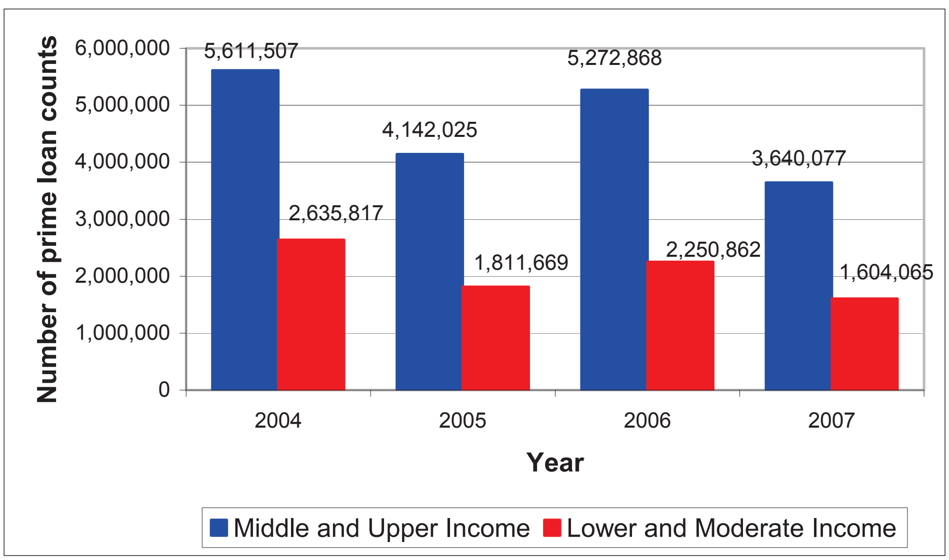
Caption: During this period, the monetary value of prime loans constituted a substantial percentage of all loans originated, no less than 75.5 percent in 2005. In contrast, the monetary value of prime loans to low- and moderate-income borrowers/neighborhoods constituted a significantly lower percentage of all prime loans originated, no more than 8 percent in 2007.

Figure 3.20 presents similar results by examining the monetary value of such loans. HMDA data show that, during the period in question, the volume of prime loans made up a substantial portion of the total of all loans (subprime and prime) originated, particularly in 2004 and 2007. From a high of 89.6 percent in 2004, the monetary share of prime loans bottomed out in 2005 to 75.5 percent, but rose to 78.2 percent in 2006 and climbed to 84.2 percent in 2007.[37]

Most notably, the volume of prime loans that banking institutions and their affiliates originated to low- and moderate-income borrowers/neighborhoods within their CRA assessment areas is consistently a very small portion of all prime loan volume originated, a finding similar to that relating to prime loan counts. Such loans represented only 7 percent of the total in 2004 and 2005, 6 percent in 2006, and 8 percent in 2007.[38]

The next set of Figures examines the distribution of prime mortgages between middle- and upper-income and low- and moderate-income borrowers/neighborhoods. The evidence indicates that middle- and upper-income individuals were the primary recipients of prime mortgage loans.

Figure 3.21
Distribution of Prime Mortgage Loans (Loan Counts) by Income of Borrowers and/or Neighborhood, 2004–2007



Note: Restricted to conventional first liens on home purchase and refinance loans for owner-occupied properties.

---

[37] The figure for each year is obtained by calculating the percentage that the total volume prime loans constituted of the total volume of subprime and prime loans originated.

[38] The figure for each year is obtained by calculating the percentage that the total volume of prime loans banking institutions and their affiliates originated to low- and moderate-income borrowers/neighborhoods within their CRA assessment areas constituted of the total volume of prime loans originated.

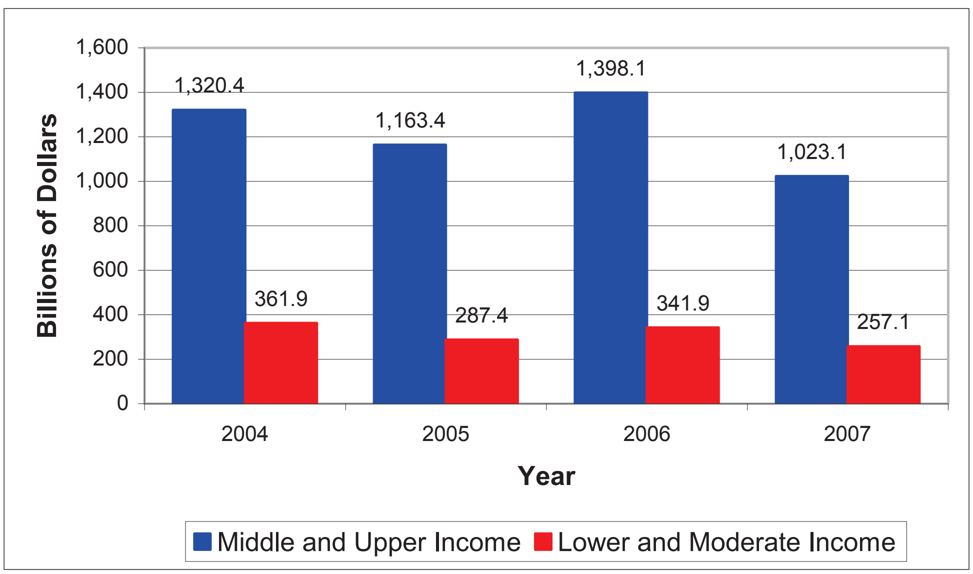
Source: "Statistics on Mortgage Lending from HMDA Data," EXCEL spreadsheet, Glenn B. Canner, The Federal Reserve, senior advisor, to Sock-Foon C. MacDougall, social scientist, U.S. Commission on Civil Rights, Feb. 19, 2009, 1:33 pm.

Caption: During this period, more than twice the number of prime loans was made to middle- and upper-income borrowers/neighborhoods than to low and moderate ones.

As reflected in Figure 3.21, financial institutions consistently originated a higher number of prime loans to middle- and upper-income borrowers. During each of the four years examined, the number of prime mortgage loans made to middle- and upper-income borrowers/neighborhoods was more than twice that to low- and moderate-income borrowers/neighborhoods.

Figure 3.22 examines similar information with regard to the volume of such loans. While Figure 3.21 indicated that middle- and upper-income borrowers/neighborhoods received the largest number of prime loans, Figure 3.22 reflects that the monetary value of such loans is even greater, with the monetary value of loans to middle- and upper-income borrowers/neighborhoods often exceeding three times the value of such loans to low- and moderate-income borrowers/neighborhoods.

Figure 3.22
Prime Mortgage Loan Volume (Billions of Dollars) by Income of Borrowers and/or Neighborhood Income, 2004–2007



Note: Restricted to conventional first liens on home purchase and refinance loans for owner-occupied properties.

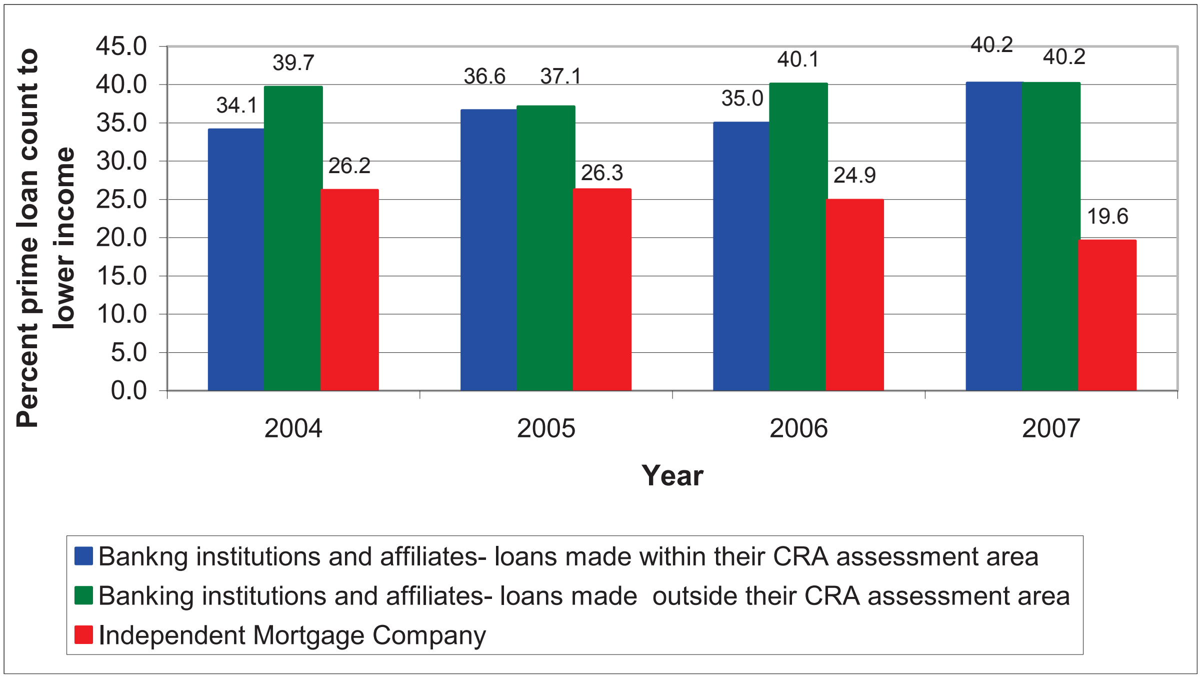
Source: "Statistics on Mortgage Lending from HMDA Data," EXCEL spreadsheet, Glenn B. Canner, senior advisor, The Federal Reserve, to Sock-Foon C. MacDougall, social scientist, U.S. Commission on Civil Rights, Feb. 19, 2009.

Caption: For this period, the monetary value of prime loans to middle and upper income borrowers/neighborhood exceeds that to low and moderate ones by more than three times.

In sum, as was the case with subprime lending, CRA-related prime loans made up only a minor part of the market, and the largest number and value of prime loans went to middle- and upper-income borrowers/neighborhoods.

The next series of Figures examines the extent to which prime loans made to low- and moderate-income borrowers/neighborhoods occur within CRA assessment areas. As reflected in Figure 3.23, and in this case unlike the situation with subprime loans,[39] the percentage of prime loans made within a CRA assessment area is very similar to those made outside the CRA assessment area.

Figure 3.23
Percent Distribution of Prime (Lower-Priced) Mortgage Loans (Loan Counts) to Low- and Moderate-Income Borrowers and/or Neighborhoods by Lender Type, 2004–2007



Note: Restricted to conventional first liens on home purchase and refinance loans for owner-occupied properties.

Source: "Statistics on Mortgage Lending from HMDA Data," EXCEL spreadsheet, Glenn B. Canner, senior advisor, The Federal Reserve, to Sock-Foon C. MacDougall, social scientist, U.S. Commission on Civil Rights, Feb. 19, 2009.

Caption: Banking institutions and their affiliates made similar percentages of prime loans within and outside their CRA assessment areas while independent mortgage companies made the least, no more than 26.3 percent.

In the case of prime loans, the percentages originated to low- and moderate-income borrowers/neighborhoods within and outside the CRA assessment areas were generally similar. Loans made within CRA assessment areas ranged from 34.1 to 40.2 percent of the total, while loans made outside the areas ranges from 37.1 to 40.2 percent. In contrast, the independent mortgage companies, which focused primarily on subprime lending, originated the lowest percentages of prime loans, which decreased steadily over time from 26.2 percent in 2004 to 19.6 percent in 2007.

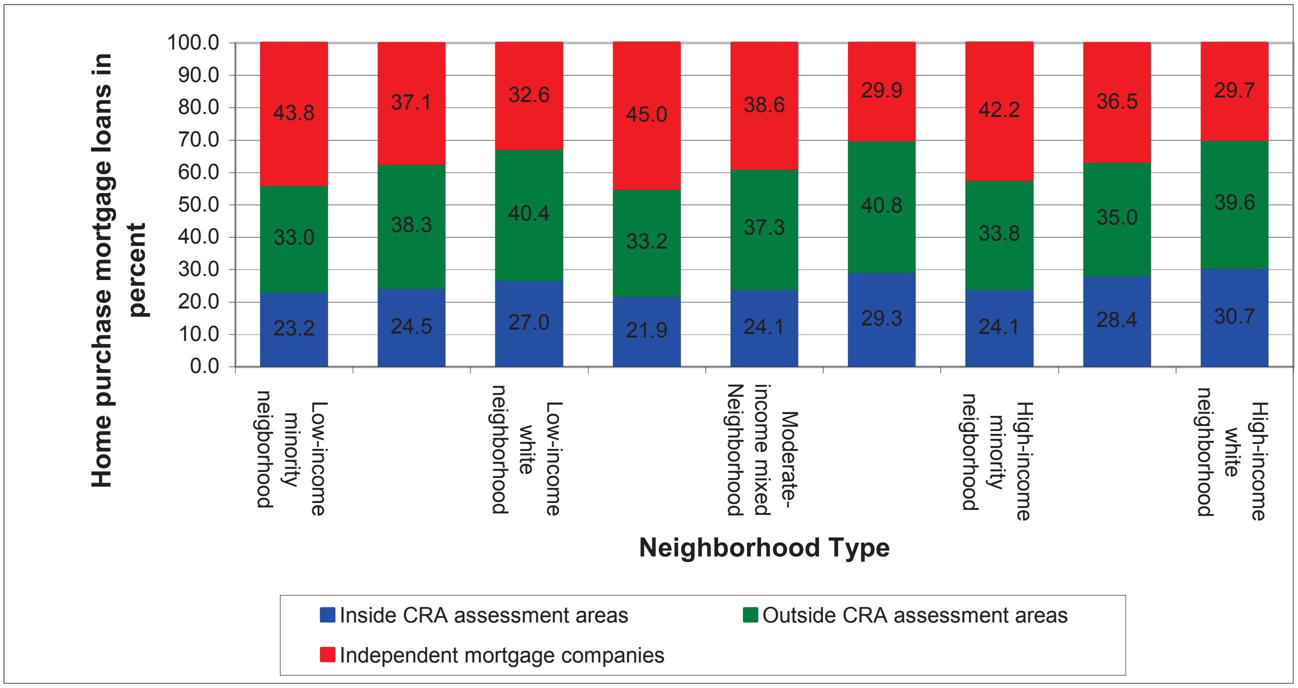
---

[39] *See* Figure 3.18.

E. Mortgage Lending by Neighborhood Income, 2006

Figures 3.24 to 3.25 take a snapshot of mortgage lending in neighborhoods with different mixes of racial/ethnic populations and income levels for the year 2006. Figure 3.24 reviews home purchase lending.

Figure 3.24
Home Purchase Mortgage Loans by Type of Neighborhood Income, 2006



Note: First-lien loans for owner occupied properties only. The small share of loans originated by credit unions is included in "outside assessment area" totals.

Source: Ren S. Essene and William C. Apgar, "The 30th Anniversary of the CRA: Restructuring the CRA to Address the Mortgage Finance Revolution," *Revisiting the CRA: Perspectives on the Future of the Community Reinvestment Act*, A Joint Publication of the Federal Reserve Banks of Boston and San Francisco, February 2009, p. 23 exhibit 2: Assessment Area Lending Lags in Low-income and Minority Areas. The source of the raw data for Exhibit 2 is the JCHS enhanced HMDA database, 2006.

Caption: In 2006, banking institutions and their affiliates were less likely to make home purchase mortgage loans within CRA assessment areas irrespective of the racial/ethnic composition and income level of the neighborhoods. Independent mortgage companies were more likely to make the highest percentage of home purchase mortgage loans in minority neighborhoods regardless of income level.

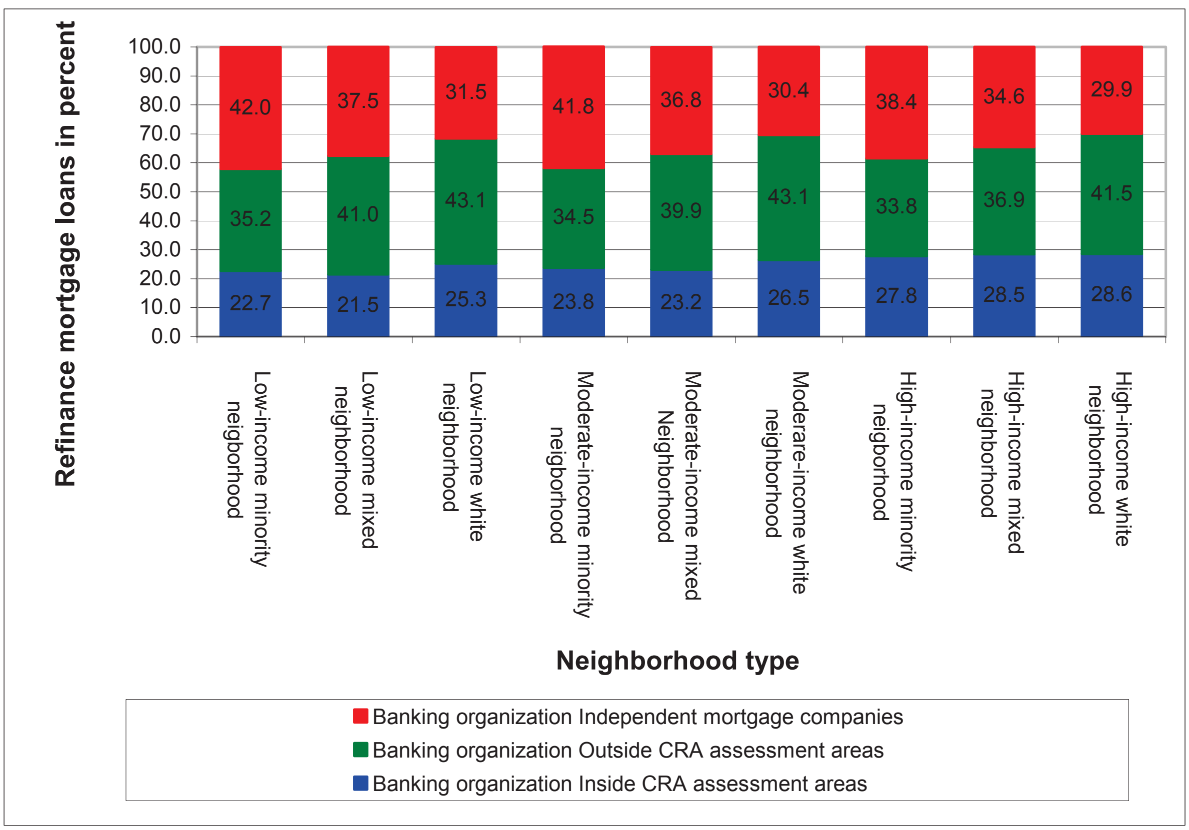
As reflected in Figure 3.24, in 2006, irrespective of the racial composition and income level of neighborhoods, banking institutions and their affiliates were still less likely to make home purchase loans within their CRA assessment areas than outside them. For example, of the total number of loans made in low-income minority neighborhoods, banking institutions and their affiliates originated 23.2 percent within their assessment areas compared to 33.0 percent outside of them. Among the loans made in moderate-income White neighborhoods, banking institutions and their affiliates originated 29.3 percent within their CRA assessment areas compared to 40.8 percent outside of them. Across the nine types of racial/ethnic income neighborhoods, the proportions of home purchase loans within CRA assessment areas were narrowly bounded, between 21.9 and 30.7 percent, a range of just 8.8 percentage points.

Of greatest significance, the percentages of home purchase loans originated by banking institutions and their affiliates within their CRA assessment areas to minority neighborhoods were the lowest compared to other types of racial/ethnic neighborhoods irrespective of income level. For example, in low-income neighborhoods, the percentage of loans to minorities was 23.2 percent compared to 24.5 percent and 27.0 percent to mixed neighborhoods and White neighborhoods, respectively. In moderate-income neighborhoods, the comparable figures were 21.9 percent in minority neighborhoods matched against 24.1 percent and 29.3 percent in mixed and White neighborhoods respectively. Similarly, in high income neighborhoods, the percentage of loans to minority neighborhoods was 24.1 percent compared to 28.4 percent and 30.7 in mixed and White neighborhoods, respectively.

Tellingly, independent mortgage companies are most likely to make the highest percentage of house purchase loans in minority neighborhoods, regardless of income level.

Figure 3.25 reviews similar information with regard to refinance mortgage lending. Again, the figures only relate to a single year, 2006.

Figure 3.25
Refinance Mortgage Loans by Type of Neighborhood Income, 2006



Note: First-lien loans for owner occupied properties only. The small share of loans originated by credit unions is included in "outside assessment area" totals.

Source: Ren S. Essene and William C. Apgar, "The 30th Anniversary of the CRA: Restructuring the CRA to Address the Mortgage Finance Revolution, Revisiting the CRA: Perspectives on the Future of the Community Reinvestment Act, A Joint Publication of the Federal Reserve Banks of Boston and San Francisco, February 2009, p. 23 exhibit 2: Assessment Area Lending Lags in Low-income and Minority Areas. The source of the raw data for Exhibit 2 is the JCHS enhanced HMDA database, 2006.

Caption: In 2006, banking institutions and their affiliates were less likely to make refinance mortgage loans within CRA assessment areas regardless of the racial/ethnic composition and income level of the neighborhoods. Independent mortgage companies were most likely to make the highest percentages of refinance mortgage loans to minority neighborhoods irrespective of income level.

As was the case of home purchase loans, irrespective of the racial composition and income levels of neighborhoods, banking institutions and their affiliates were less likely to originate refinance loans within their CRA assessment areas than outside them. However, unlike with home purchase loans, the percentages of refinance loans banking institutions and their affiliates made within their assessment areas was lowest for minority neighborhoods only in high income areas, 27.8 percent. In low- and moderate-income areas, it was racially mixed neighborhoods that received the lowest share, 21.5 percent and 23.2 percent, respectively.

Across the nine types of racial/ethnic income neighborhoods, the proportions of refinance purchase loans within CRA assessment areas are clustered closely together, between 21.5 and 28.6 percent, a range of only 7.1 percentage points.

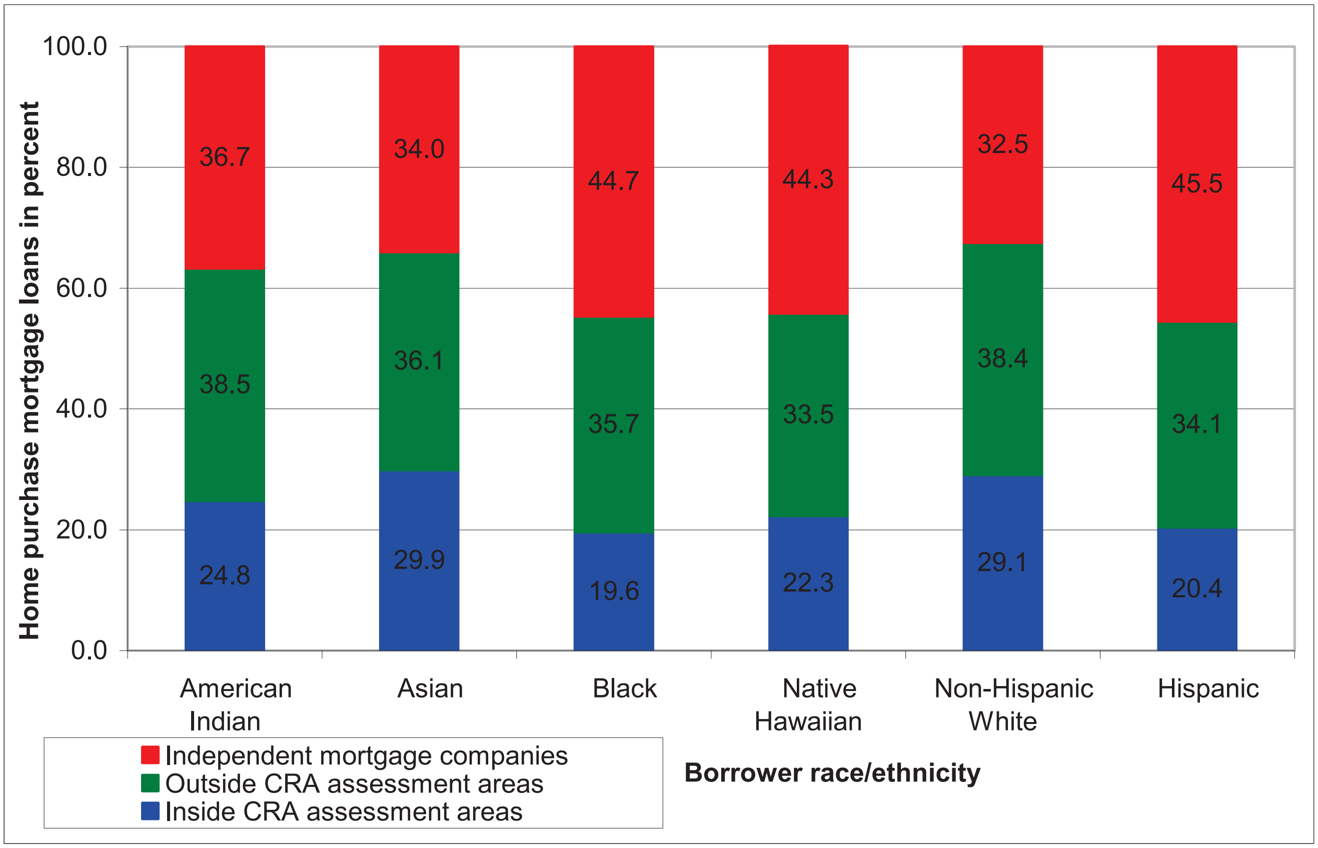
Again independent mortgage companies continued to be most likely to make the highest percentage of refinance loans in minority neighborhoods, regardless of income.

F. Mortgage Lending By Race

Figures 3.26 to 3.27 shift the focus to borrower race and ethnicity in examining home purchase and refinance lending. This analysis is particularly informative in determining the degree to which CRA loans are ultimately obtained by various racial and/or ethnic groups.

Figure 3.26 documents home purchase lending practices for the year 2006.

Figure 3.26
Home Purchase Loans by Race, 2006



Note: First-lien loans for owner occupied properties only. The small share of loans originated by credit unions is included in "outside assessment area" totals.

Source: Ren S. Essene and William C. Apgar, "The 30th Anniversary of the CRA: Restructuring the CRA to Address the Mortgage Finance Revolution, *Revisiting the CRA: Perspectives on the Future of the Community Reinvestment Act*, A Joint Publication of the Federal Reserve Banks of Boston and San Francisco, February 2009, p. 23 exhibit 2: Assessment Area Lending Lags in Low-income and Minority Areas. The source of the raw data for Exhibit 2 is the JCHS enhanced HMDA database, 2006.

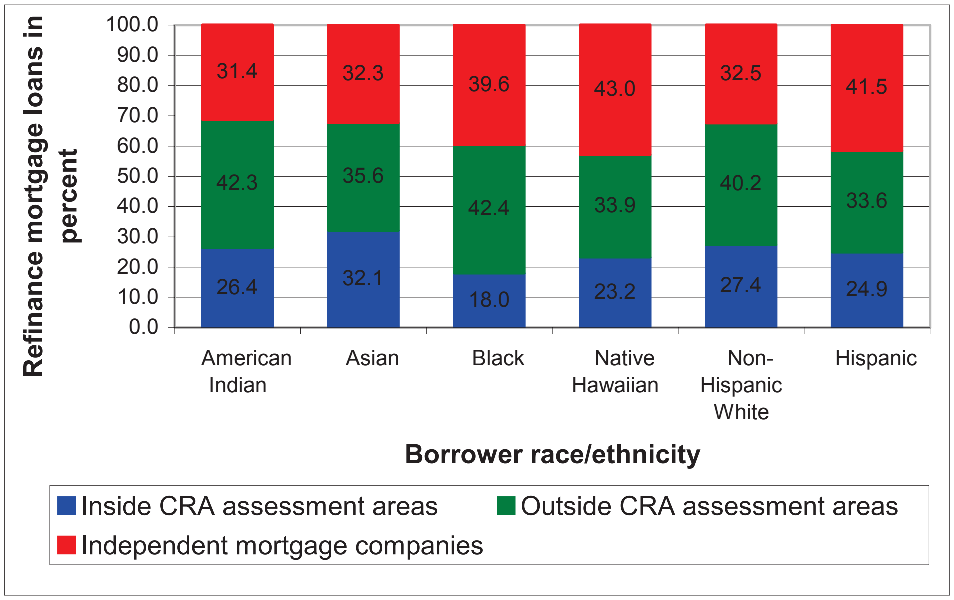
Caption: Banking institutions and their affiliates were less likely to make home purchase loans within their assessment areas regardless of the race or ethnicity of the borrowers.

The data in Figure 3.26 indicate that, in 2006, banking institutions and their affiliates were less likely to make home purchase loans within their assessment areas, irrespective of the race or ethnicity of the borrowers. For example, home purchase loans made to Blacks within CRA assessment areas equaled 19.6 percent. Such loans made outside the CRA areas, however, equaled 35.7 percent. Similar percentages apply with equal force to other groups. For Hispanics, the respective figures were 20.4 percent versus 34.1 percent; for Whites, 29.1 percent versus 38.4 percent; and for Asians/Pacific Islanders, 29.9 percent versus 36.1 percent.

While a single year is hardly determinative, for 2006, the minorities who were to most benefit from the CRA, were more likely to obtain loans from other sources.

Figure 3.27 examines the same information with regard to home refinance lending practices. Again, the figures only apply to 2006.

Figure 3.27
Home Refinance Loans by Race/Ethnicity, 2006



Note: First-lien loans for owner-occupied properties only. The small share of loans originated by credit unions are included in "outside assessment area" totals.

Source: Ren S. Essene and William C. Apgar, "The 30th Anniversary of the CRA: Restructuring the CRA to Address the Mortgage Finance Revolution," *Revisiting the CRA: Perspectives on the Future of the Community Reinvestment Act*, A Joint Publication of the Federal Reserve Banks of Boston and San Francisco, February 2009, p. 23 exhibit 2: Assessment Area Lending Lags in Low-income and Minority Areas, p. 23. The source of the raw data for Exhibit 2 is the JCHS enhanced HMDA database, 2006.

Caption: Banking institutions and their affiliates were less likely to make home refinance loans within their assessment areas regardless of the race or ethnicity of the borrowers.

Figures for refinance loans mirror those in Figure 3.26, regarding home purchase loans. In both cases, banking institutions and their affiliates were less likely to make loans within their CRA assessment areas, regardless of the race or ethnicity of borrowers. For example, the percentage of refinance loans to Black borrowers within CRA assessment areas was 18 percent, while the percentage of such loans outside the area was 42.4 percent. The respective figures for Hispanics were 24.9 percent and 33.6 percent, while the percentages for Whites were 27.4 percent and 40.2 percent.

VI. HUD's Lending Goals

This next section examines the performance of GSEs generally, and Fannie Mae and Freddie Mac in particular, with regard to HUD's lending goals. First, this section examines performance of Fannie Mae and Freddie Mac against the HUD lending goals. These reflect that, until the market began to collapse, the goals were being met.

The section then examines the number of loans purchased by Fannie Mae and Freddie Mac involving minority borrowers. These figures reflect that most minority groups, including Hispanics and Blacks, received increasingly larger proportions of loans from Fannie Mae and Freddie Mac during the period examined. When such figures were compared with loans involving White borrowers, the analysis demonstrates that the purchases by Fannie Mae and Freddie Mac roughly followed the same pattern for all groups. This is so both with regard to when the market was rising, as well as when the market began to tighten.

Finally, this section examines the GSEs' performance overall during the housing boom and bust. This section reflects that, while the GSEs' share of the subprime market increased over time, other players in the secondary market vastly outpaced the GSEs' purchase of subprime loans.

Overall, the analysis contained in this section reflects that the GSEs' growth mirrored the growth in homeownership from 2000 to 2004. Thereafter, the GSEs' share of the market experienced a substantial drop.

As far as minority lending, both the number and monetary volume of loans purchased by the GSEs from minorities mirrored the overall growth of homeownership. At all stages, however, the overwhelming majority of loans purchased by GSEs were to Whites.

As discussed more fully in Chapter 2, in 1992 Congress established oversight responsibilities for HUD to ensure the GSEs' compliance with their charters. Among these responsibilities was the obligation to encourage lending to low- and moderate-income families. Prior to 1995, these goals had to be met by the GSEs directly. In 1995, however, HUD allowed GSEs to receive affordable housing credits by buying securities from third parties that included loans to low-income borrowers. Such purchased loans could be held by the GSEs in their own portfolios. This section includes analysis of such purchases.

Table 3.1 reflects HUD's housing goals and home purchase subgoals for the period from 1996 through 2007.[40] As indicated, the goals in question increased significantly over this period. For example, the low- and moderate-income goal was at 40 percent in 1996. It was then increased to 42 percent from 1997 through 2000, and was increased again, to 50 percent, for 2001 to 2004. The goal then increased yet again: to 52 percent in 2005; 53 percent in 2006; and 55 percent in 2007. This constituted an increase in the goal of 15 percentage points in a little over a decade. The increase in the geographically-targeted goal was even more dramatic, increasing from 21 percent in 1996 to 38 percent in 2006, an increase of 17 percentage points.

Table 3.1 shows HUD's housing goals and home purchase subgoals except for the multifamily goal, which is not relevant to this study.

---

[40] HUD housing goals are for home purchase and refinancing mortgages. The subgoals, which were imposed for the first time in 2005, are for home purchases only.

Table 3.1
Levels of the Department of Housing and Urban Development's Lending Goals and Subgoals for Government-Sponsored Enterprises Since 1996 by Year

HOUSING GOALS	YEAR											
	1996	1997	1998	1999	2000	2001	2002	2003	2004	2005	2006	2007
Low- and Moderate-Income Goal	40%	42%	42%	42%	42%	50%	50%	50%	50%	52%	53%	55%
Geographically Targeted (Underserved Area) Goal	21%	24%	24%	24%	24%	31%	31%	31%	31%	37%	38%	38%
Special Affordable Goal	12%	14%	14%	14%	14%	20%	20%	20%	20%	22%	23%	25%
HOME PURCHASE SUBGOALS												
Low- and Moderate-Income Subgoal										45%	46%	47%
Geographically Targeted (Underserved Area) Subgoal										32%	33%	33%
Special Affordable Subgoal										17%	17%	18%

Source: Sources: U.S. Department of Housing and Urban Development, Office of Policy Development and Research, *Profiles of GSE Mortgage Purchases in 1999 and 2000*, April 2002, p. 8 table 1; U.S. Department of Housing and Urban Development, Office of Policy Development and Research, *Profiles of GSE Mortgage Purchases in 2001-2004*, April 2008, p. 9 table 1; U.S. Department of Housing and Urban Development, Office of Policy Development and Research, *Profiles of GSE Mortgage Purchases in 2005-2007*, September 2008, pp. 9–10 tables 1a & 1b.

Caption: Between 1996 and 2007, HUD's goals for government-sponsored enterprises increased from 40 to 55 percent of mortgage lending to low- and moderate- income individuals, from 21 to 38 percent of home loans to borrowers in geographically targeted (i.e., underserved) areas, and from 12 to 25 percent to purchasers of special affordable housing. HUD introduced subgoals in 2005 and have increased them slightly since then, with the low-and moderate- income subgoal rising from 45 to 47 percent, the geographically targeted (underserved area) subgoal going from 32 to 33 percent, and the special affordable subgoal from 17 to 18 percent.

The GSEs' performance against the HUD lending goals can be measured through annual loan-level data (provided by the GSEs to HUD) that includes detailed mortgage characteristics for all of their purchase transactions. This GSE database allows analysis of financial, borrower, and locational characteristics of GSE loan purchases and changes in GSE performance over time. HUD also uses this database to verify HMDA-reported data on GSE purchases.[41]

---

[41] *See, ,e.g.,* Harold L. Bunce and Randall M. Scheessele, *The GSEs' Funding of Affordable Loans: A 1996 Update* (Office of Policy Development and Research, U.S. Department of Housing and Urban Development, Housing Finance Working Paper

Insight into GSE performance as compared to the primary market, including portfolio lenders such as banks and thrifts, is possible via examination of HMDA data. The data provide information on both primary market originations and secondary market purchases.[42] The data indicate GSEs' goal-qualifying home purchase and refinance mortgages involving borrowers with (1) very low income, (2) "special affordable" qualifications (i.e., very low income or low-income living in low-income census tracts), (3) less than area median income, and (4) residences in underserved areas.[43]

HMDA data include more types of loans than may be appropriate in evaluating GSE performance. HMDA data include investor loans and manufactured housing loans. Indeed, manufactured home loans generally do not meet the GSEs' underwriting standards. Thus, Fannie Mae and Freddie Mac argue that they should not be included when comparing GSEs to the rest of the market. Similar arguments arise over whether below-investment-grade loans, also represented in HMDA data, should be counted in comparisons.[44]

A. GSEs' Performance Against the HUD Goals

Figure 3.28 shows the HUD goals, and Fannie Mae and Freddie Mac's performance against them, for 1996 through 2007. These include: (i) the goals for low- and moderate-income lending; (ii) the geographically-targeted or underserved area goals; and (iii) the special affordability goal.

In addition, it shows Fannie Mae and Freddie Mac's level of performance for three prior years (1993 to 1995) of a transition period. During this period HUD was monitoring performance against three goals, only two of which are the same as those established in 1996 and thereafter.[45]

Series, Working Paper No. HF-005, July 1998, p. 7 (hereinafter cited as Bunce and Scheessele, *GSEs' Funding of Affordable Loans*).

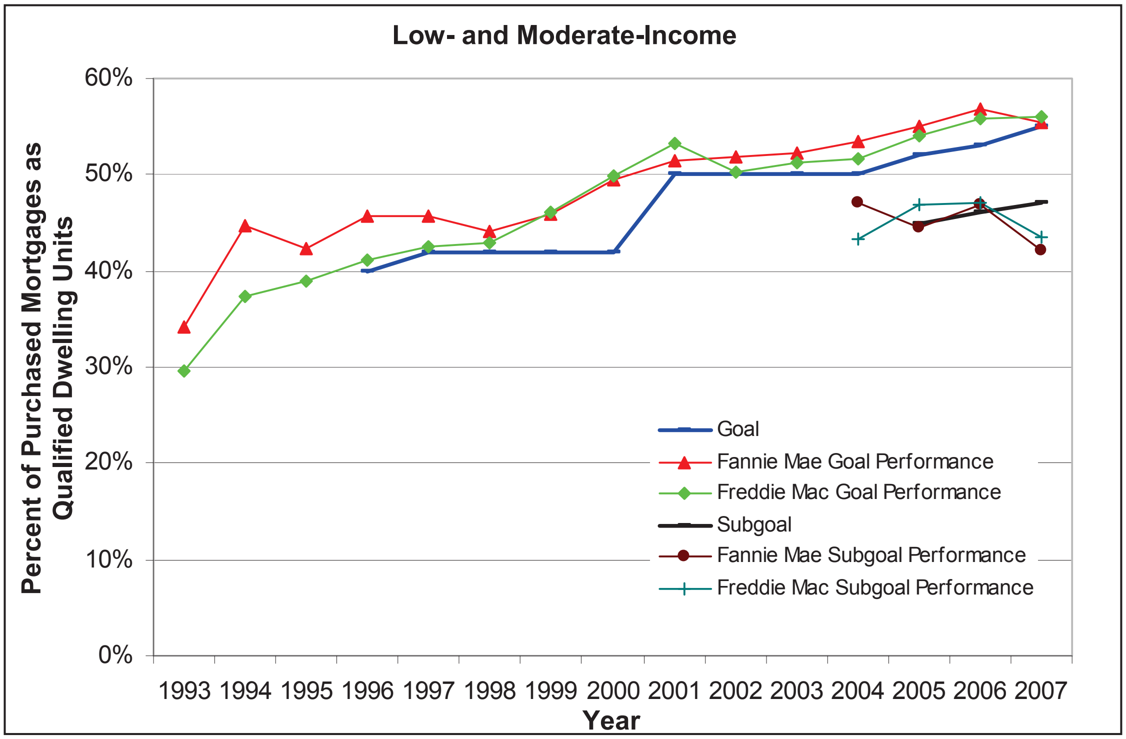
[42] *Id.*

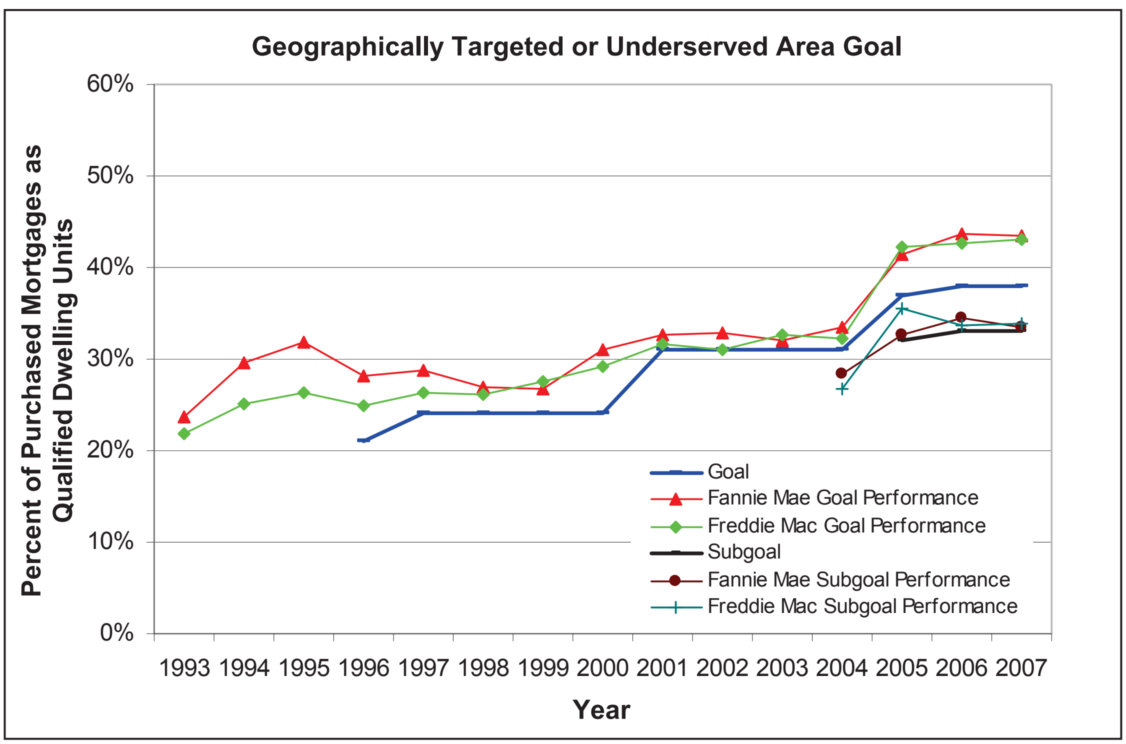
[43] *See, e.g.,id.* at pp. 11–12 tables 2a & 2b.

[44] Bunce and Scheessele, *GSEs' Funding of Affordable Loans* at p. 8.

[45] *See, e.g.*, Paul B. Manchester, Sue George Neal, and Harold L. Bunce, *Characteristics of Mortgages Purchased by Fannie Mae and Freddie Mac,* 1993-95 (Office of Policy Development and Research, U.S. Department of Housing and Urban Development, Housing Finance Working Paper Series, Working Paper No. HF-003, p. 6). A central city goal was an early predecessor of the geographically targeted goal. *See, e.g.,* Paul B. Manchester, Sue George Neal, and Harold L. Bunce.

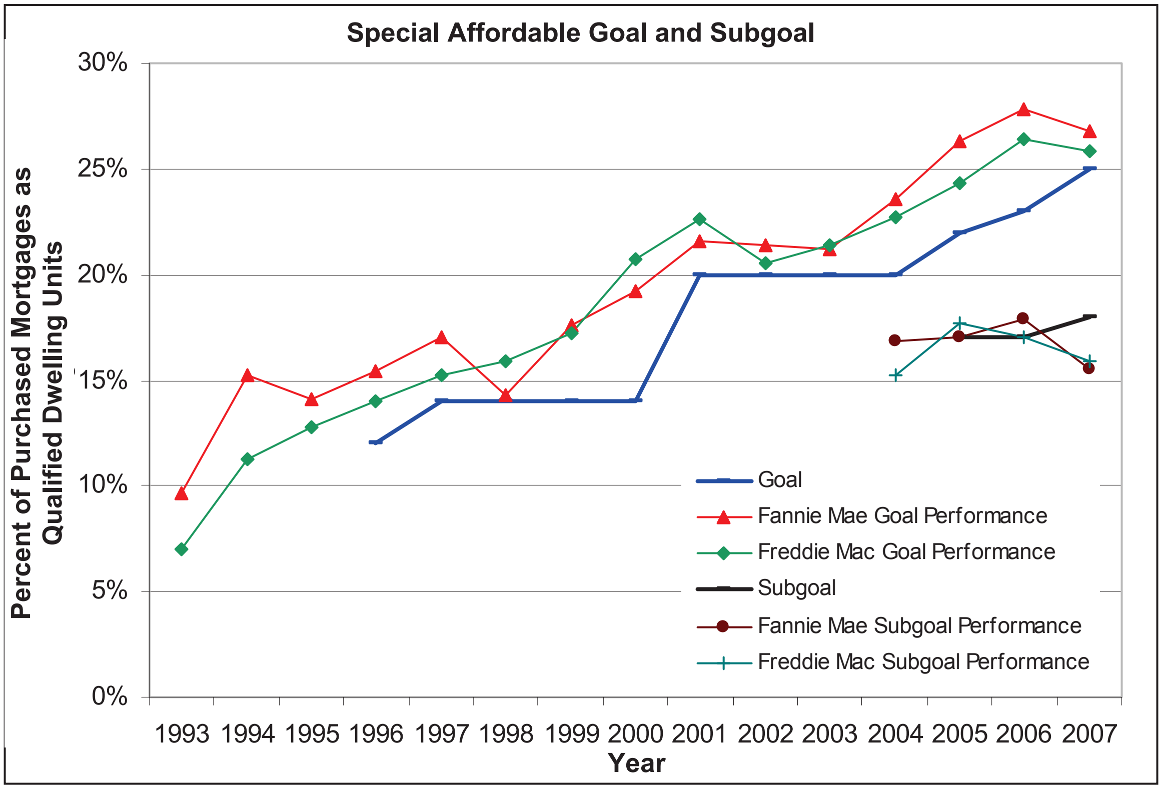
Figure 3.28
Fannie Mae and Freddie Mac's Performance Against the Department of Housing and Urban Development's Lending Goals and Subgoals, 1993–2007





(continued)

Figure 3.28 (continued)
Fannie Mae and Freddie Mac's Performance Against the Department of Housing and Urban Development's Lending Goals and Subgoals, 1993–2007



Sources: U.S. Department of Housing and Urban Development, Office of Policy Development and Research, *Profiles of GSE Mortgage Purchases in 1999 and 2000*, April 2002, p. 8 table 1; U.S. Department of Housing and Urban Development, Office of Policy Development and Research, *Profiles of GSE Mortgage Purchases in 2001-2004*, April 2008, p. 9 table 1; U.S. Department of Housing and Urban Development, Office of Policy Development and Research, *Profiles of GSE Mortgage Purchases in 2005-2007*, September 2008, pp. 9–10 tables 1a & 1b.

Caption: With HUD's increases in the GSEs' goals from 1996 to 2007, Fannie Mae and Freddie Mac have consistently performed above the goals for mortgage lending to low- and moderate-income borrowers, those in geographically targeted or underserved areas, and those buying special affordable housing. In 2007, Fannie Mae and Freddie Mac's performance dropped below the HUD subgoals for low- and moderate-income borrowers, and those purchasing special affordable housing.

As reflected in Figure 3.28, both Fannie Mae and Freddie Mac were able to meet goals for low- and moderate-income lending, geographically-targeted or underserved area goals, as well as the special affordable goal during the time period in question. More difficulty, however, was experienced with regard to the subgoals, especially as the mortgage market began its collapse.

B. GSEs' Efforts to Increase Minority Homeownership

As indicated previously, the HUD goals were designed to increase the number of mortgages issued to low- and moderate-income families, those living in underserved areas, or special affordable housing families. This section views the effects of the GSEs' performance against these goals in terms of increases in mortgages to members of minority groups.

For this report, the government-sponsored enterprises collectively include those reported in HMDA data: Fannie Mae, Freddie Mac, the Government National Mortgage Association (Ginnie Mae), and the Federal Agricultural Mortgage Corporation (Farmer Mac). Of these, this report presents detailed information on Fannie Mae and Freddie Mac, which are the largest two.

The GSEs purchase mortgages from primary lenders and either hold the mortgages in portfolio or sell them to other investors as mortgage-backed securities, with a guarantee that the investors will receive full and timely payment of principal and interest.[46] Their underwriting standards play a dominant role in determining the types of loans that primary lenders will originate in the conventional conforming market.[47]

The required data reporting under HMDA is designed to show whether financial institutions are serving the housing credit needs of their neighborhoods and communities and to help identify possible discriminatory lending patterns. This effort yields information about banks' and other financial institutions' annual loan activities—the applications for financing they receive and the loans they originate or purchase from other lenders—for mortgages to buy, improve, or refinance homes.[48]

The GSEs do not originate mortgages. They purchase the loans that other financial institutions originated or purchased. The Figures that follow will show, by year, the loans that Fannie Mae and Freddie Mac, or collectively all GSEs, purchased, regardless of whether the financial institution selling them to the GSE originated or purchased them.

---

[46] *See, e.g.,* Harold L. Bunce, *The GSEs' Funding of Affordable Loans: A 2000 Update* (Office of Policy Development and Research, U.S. Department of Housing and Urban Development, Housing and Urban Development, Housing Finance Working Paper Series, Working Paper No. HF-013, April 2002, p. 3 (citing for explanations of the overall role of Fannie Mae and Freddie Mac in the secondary mortgage market, the following studies: Congressional Budget Office, *Assessing the Public Costs and Benefits of Fannie Mae and Freddie Mac,* May 1996; U.S. Department of Housing and Urban Development, *Privatization of Fannie Mae and Freddie Mac: Desirability and Feasibility, A HUD Report,* July 1996; U.S. Department of Treasury, *Government Sponsorship of the Federal National Mortgage Association and the Federal Home Loan Mortgage Corporation,* July 1996).

[47] *See, e.g*, *id.* (citing for discussions of the GSEs' underwriting standards the following studies: RUTGERS UNIVERSITY, CENTER FOR URBAN POLICY RESEARCH, SUCCESSFUL MORTGAGE LENDING STRATEGIES FOR THE UNDERSERVED (November 1998), a report to the U.S. Department of Housing and Urban Development; THE URBAN INSTITUTE, A STUDY OF THE GSES' SINGLE FAMILY UNDERWRITING GUIDELINES (February 1999), a report prepared for the U.S. Department of Housing and Urban Development, Office of Policy Development and Research; and Robert Van Order and Ann B. Schnare, *Finding Common Ground*, SECONDARY MORTGAGE MARKET, vol. 11, no. 1 (Winter 1994), at pp. 1, 15–19).

[48] Federal Financial Institutions Examination Council, *A Guide to HMDA Reporting: Getting It Right,* Jan. 1, 2008, p. 1, available at <http://www.ffiec.gov/hmda/guide.htm> (last accessed Aug. 3, 2009). A financial institution, whether depository or nondepository, must report HMDA data if it engages in residential mortgage lending and exceeds certain minimums for amount of business in metropolitan areas and size. Also, depository institutions, for example, must report a loan in HMDA data when they are federally insured or regulated; use a federal agency to insure, guarantee, or supplement the loan; or intend to sell the loan to Fannie Mae or Freddie Mac. *Id.* at p. 3.

Figure 3.29 indicates, by year, the percentage of loans the GSEs purchased apportioned among minority borrowers. The Figure shows only loans of borrowers for whom racial or ethnic information was available in HMDA data. In addition, only the main racial or ethnic categories are reflected. Those designated as “other,” or who provide multiple designations, are not included. Whites, who are not shown in the figure, received approximately 80 to 90 percent of the loans that GSEs purchased. Regardless of year, no minority group received more than 10.4 percent of the loans whether purchased by Fannie Mae, Freddie Mac, or all four GSEs.

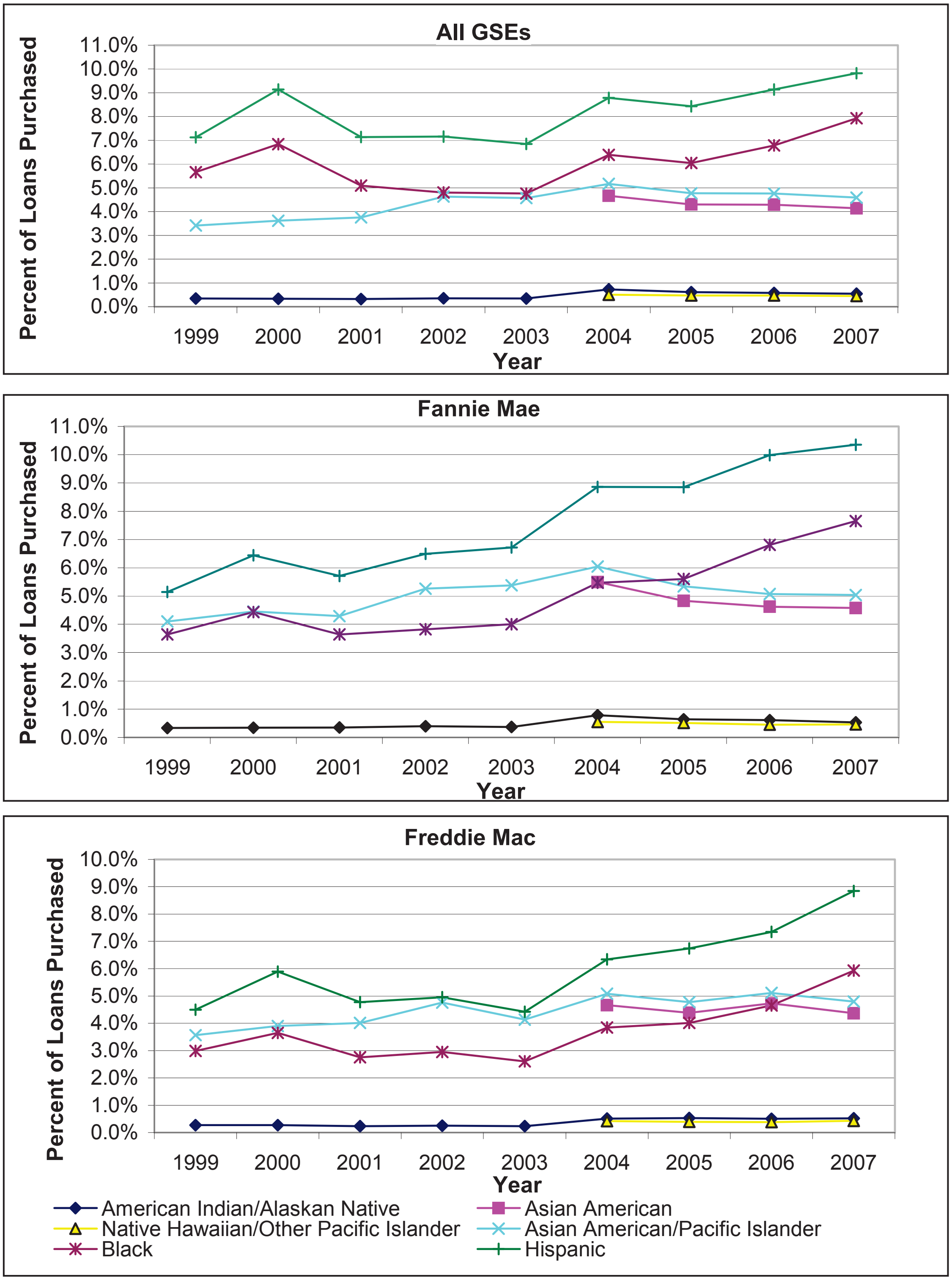
From 1999 to 2007, and particularly from 2004 through 2007, Hispanics and Blacks received increasingly larger proportions of the loans that Fannie Mae and Freddie Mac purchased. For example, the percentage of loans Fannie Mae purchased of Hispanic borrowers was 5.1 percent in 1999 and, after a rise and fall in 2000 and 2001, continued to increase from 5.7 percent to 10.4 percent in 2007. In a similar fashion, the percentage of loans that Fannie Mae purchased involving Black borrowers was 3.6 percent in 1999 and, after rising and falling to the same level in 2001, continuously increased to 7.7 percent in 2007.

The percentage of loans that Freddie Mac purchased of Hispanic borrowers rose steadily since 2003 to a level of 8.8 percent in 2007. The percentage of loans that Freddie Mac purchased involving Black borrowers was 3.0 percent in 1999. It rose and fell, decreasing to 2.6 percent in 2003, and then increased thereafter, reaching 5.9 percent in 2007.

The percentage of loans Fannie Mae and Freddie Mac purchased involving Asian Americans or Pacific Islanders did not increase in recent years. From 2002 through 2007, the proportion of loans purchased of Asian-American borrowers fluctuated between 4.1 and 5.1 for Freddie Mac and between 5.0 and 6.0 for Fannie Mae. For 2004 through 2007, the figure depicts Native Hawaiians and other Pacific Islanders separately from Asian Americans. In each of the years shown, about half of a percent of the loans Fannie Mae and Freddie Mac purchased involved Native Hawaiians and other Pacific Islanders.

Of the loans Fannie Mae and Freddie Mac purchased, American Indians and Alaskan Natives were involved in between 0.2 and 0.4 percent in 1999 to 2003 and 0.5 and 0.8 percent in 2004 through 2007.

Figure 3.29
GSEs' Purchased Loans (of Institutions' Originations and Purchased Ones) Apportioned by Race/Ethnicity of Minority Borrowers, 1999–2007



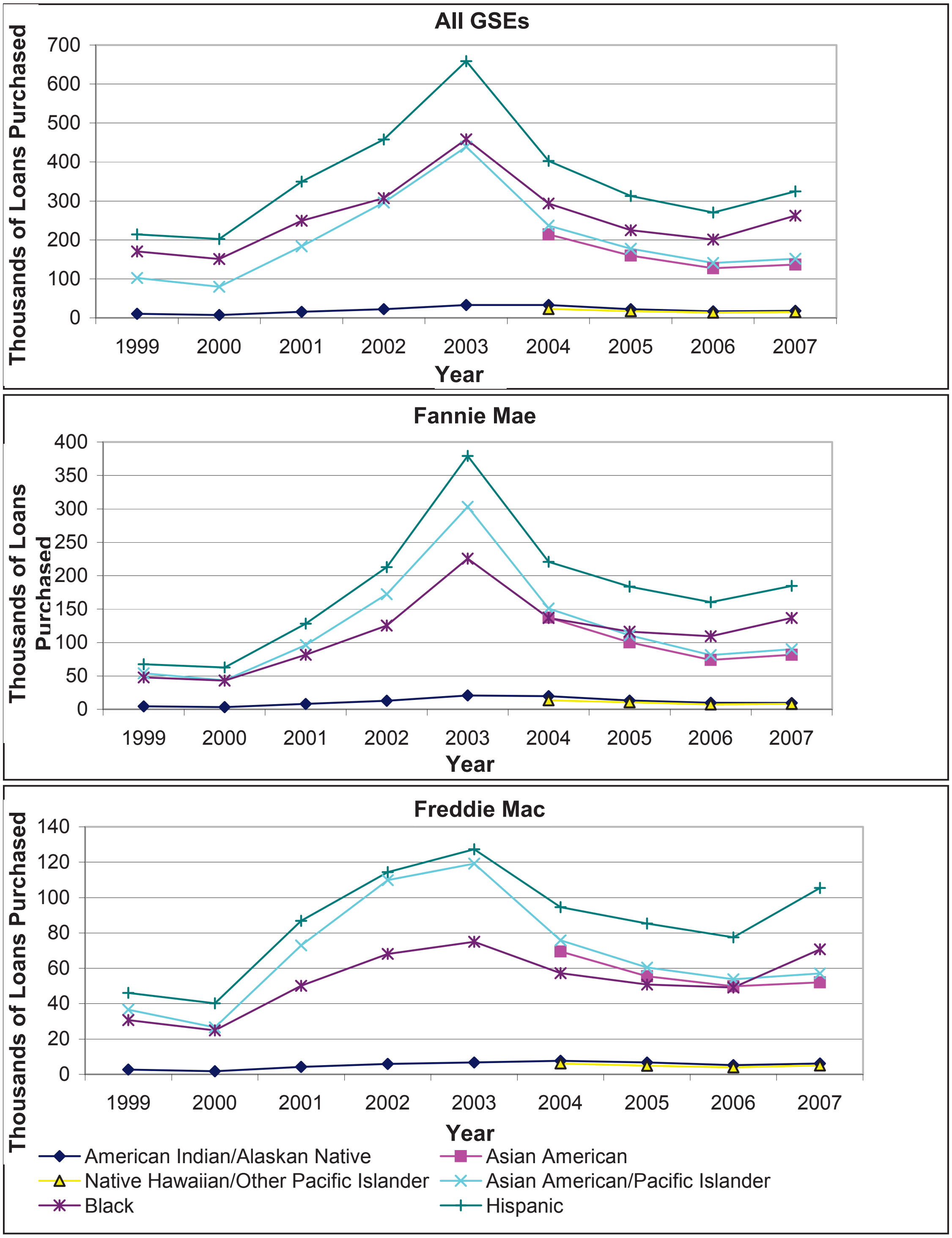
Note: The category “All GSEs” includes Fannie Mae, Freddie Mac, Ginnie Mae, and Farmer Mac. Figures exclude borrowers for whom race was "2 or more minority races," "joint (white/minority)," "other," or unavailable. Note further that because of the manner in which HMDA data was collected, “Hispanics” are treated as a racial category in 1999 to 2003. In 2004 to 2007, “Hispanics” are an ethnicity, distinguished from non-Hispanics, but they are also counted in the racial categories as “White,” “Black,” etc., where appropriate.

Source: Compiled by the U.S. Commission on Civil Rights using HMDA data, tables 3 or 3.1 for 1999 to 2007.

Caption: From 1999 to 2007, Hispanics made up the highest percentage of minority borrowers among the loans purchased, whether by all four GSEs (ranging from about 7 to 10 percent), Fannie Mae, or Freddie Mac. Loans to Black borrowers comprised approximately 5 to 8 percent of those the GSEs purchased; home loans to Asian American/Pacific Islanders were roughly 3 to 5 percent; and those to American Indian/Alaskan Natives were always less than one percent. Indeed, the percentage of Fannie Mae and Freddie Mac’s purchased loans to Hispanics and Blacks increased, particularly from 2003 through 2007, while the percentage of purchased loans to Asian Americans, Pacific Islanders, and American Indians and Alaskan Natives remained relatively level during these years.

While Figure 3.29 looked at percentages, Figure 3.30 examines the number of loans the GSEs purchased of those which other financial institutions originated with minority borrowers. As reflected in Figure 3.30, the actual number of such minority loans fluctuated greatly over the time period in question.

Figure 3.30
Counts of GSEs' Loans (of Institutions' Originations and Purchased Ones) Involving Minority Borrowers, 1999–2007



Note: “All GSEs” includes Fannie Mae, Freddie Mac, Ginnie Mae, and Farmer Mac. Figures exclude borrowers for whom race was "2 or more minority races," "joint (white/minority)," "other," or unavailable. Note further that because of the manner in which HMDA data was collected, “Hispanics” are treated as a racial category in 1999 to 2003. In 2004 to 2007, “Hispanics” are an ethnicity, distinguished from non-Hispanics, hence their loans are also counted in the racial categories as “White,” “Black,” etc., where appropriate.

Source: Compiled by the U.S. Commission on Civil Rights using HMDA data, tables 3 or 3.1 for 1999 to 2007.

Caption: All GSEs and Fannie Mae dramatically increased the hundreds of thousands of purchased loans to Black, Hispanic, and Asian American/ Pacific Islander borrowers in 2003. Freddie Mac increased purchases of minority loans too, but more gradually, spanning a period from 2001 to 2003. After 2003, the GSEs (either in total or for the two largest ones) decreased (by hundreds of thousands) the purchased loans to minorities through 2006, then increased from 2006 to 2007, with an exception of their purchased mortgages to American Indian/Alaskan Natives, which were small but steady throughout.

The Figure shows that the number of loans the GSEs purchased that involved Hispanic, Asian American and Pacific Islander, and Black borrowers, decreased slightly from 1999 to 2000, increased sharply from 2000 to 2003, then declined through 2006 before increasing again in 2007. This same trend occurs for Fannie Mae’s purchases, Freddie Mac’s, and all GSEs collectively.

Both Fannie Mae and Freddie Mac (and the GSEs as a whole) purchased more loans of Hispanic borrowers than any other minority racial/ethnic group throughout the period. All four GSEs purchased 214,312 loans of Hispanic borrowers in 1999 and 202,111 in 2000. The number grew to 658,713 in 2003, then waned to 270,651 in 2006. It ended at 324,653 in 2007. In the peak year of 2003, Fannie Mae purchased 379,248 loans of Hispanics and Freddie Mac, 127,311.

For both Fannie Mae and Freddie Mac, the second largest amount of purchased loans came from Asian Americans/Pacific Islanders. Fannie Mae purchased 53,853 such loans in 1999, 303,180 in 2003, and 89,823 in 2007. Freddie Mac purchased 36,591 loans of Asian American/Pacific Islander borrowers in 1999, 119,150 in 2003, and 57,158 in 2007.

Fannie Mae and Freddie Mac’s purchased loans from Blacks trailed those relating to both Hispanics and Asian Americans/Pacific Islanders. Fannie Mae purchased 47,838 loans of Blacks in 1999, 225,632 in 2003, and 136,626 in 2007. Of loans to Black borrowers, Freddie Mac purchased 30,670 in 1999, 74,992 in 2003, 49,112 in 2006. Freddie Mac did much better at purchasing loans of Blacks in 2007—reaching 70,789.

Notably, GSEs as a whole purchased more loans of Black borrowers than of Asian Americans/Pacific Islanders. This anomaly only occurred, however, because Ginnie Mae, which is not broken out in the chart, guaranteed much larger numbers of loans of Blacks relative to the few it purchased involving borrowers who were Asian Americans/Pacific Islanders.

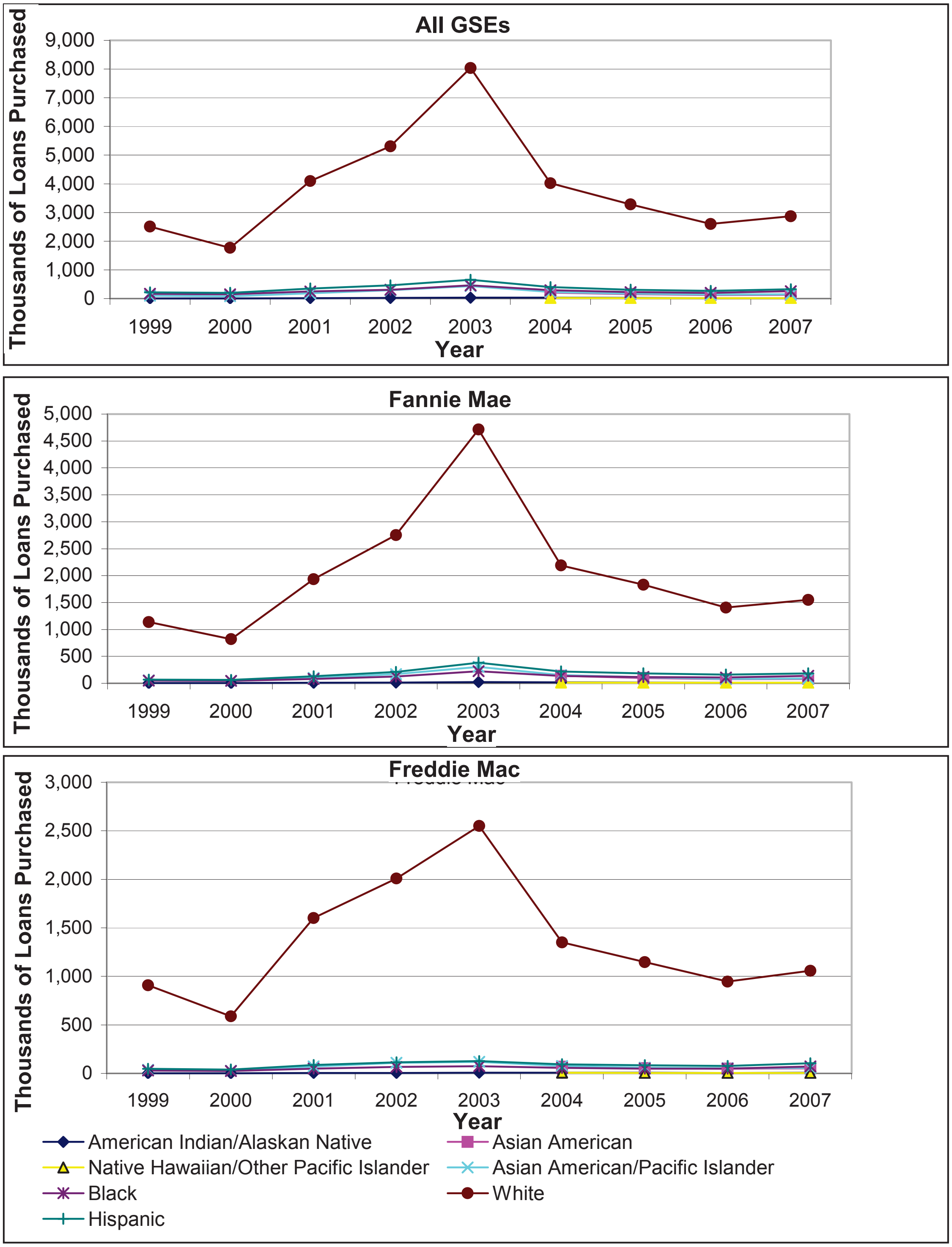
Native Americans and Alaskan Natives followed essentially the same pattern as other minorities. While their trends appear very flat, this is only because the GSEs guaranteed small numbers of their loans relative to the other groups—ranging (for all GSEs) from 7,427 in 2000, the lowest year, to 33,198 and 33,258 in 2003 and 2004, and ending with 17,977 in 2007.

Beginning in 2004, the HMDA data separate Asian Americans from Native Hawaiians and other Pacific Islanders. The Figure shows the two groups combined (which forms a continuous trend line from 1999 to 2007) and separately (for 2004 to 2007). The GSEs purchased relatively small numbers of loans made to Native Hawaiians and other Pacific Islanders—22,934 in 2004, decreasing to 13,795 in 2006, then rebounding slightly to 14,743 in 2007.

The next Figure reflects the extent of GSEs' purchase loans of minorities, but also includes White borrowers. Figure 3.31 reflects that the GSEs' purchase of loans from White borrowers was far greater than those from minority borrowers during the whole period examined.

Most significantly, the rise and decrease in purchases by GSEs roughly followed the same pattern for all groups, Whites and minorities. That is to say, purchases increased from 2000 to 2003, at which time the GSEs' purchases reached an apex. Thereafter, purchases related to all racial groups and ethnicities decreased.

Figure 3.31
Counts of GSEs' Purchased Loans (of Institutions' Originations or Purchased Ones) Involving Minority or White Borrowers, 1999–2007



Note: The category “All GSEs” includes Fannie Mae, Freddie Mac, Ginnie Mae, and Farmer Mac. Figures exclude borrowers for whom race was "2 or more minority races," "joint (white/minority)," "other," or unavailable. Note further that because of the manner in which HMDA data was collected, “Hispanics” are treated as a racial category in 1999 to 2003. In 2004 to 2007, “Hispanics” are an ethnicity, distinguished from non-Hispanics, hence their loans are also counted in the racial categories as “White,” “Black,” etc., where appropriate.

Source: Compiled by the U.S. Commission on Civil Rights using HMDA data, tables 3 or 3.1 for 1999 to 2007.

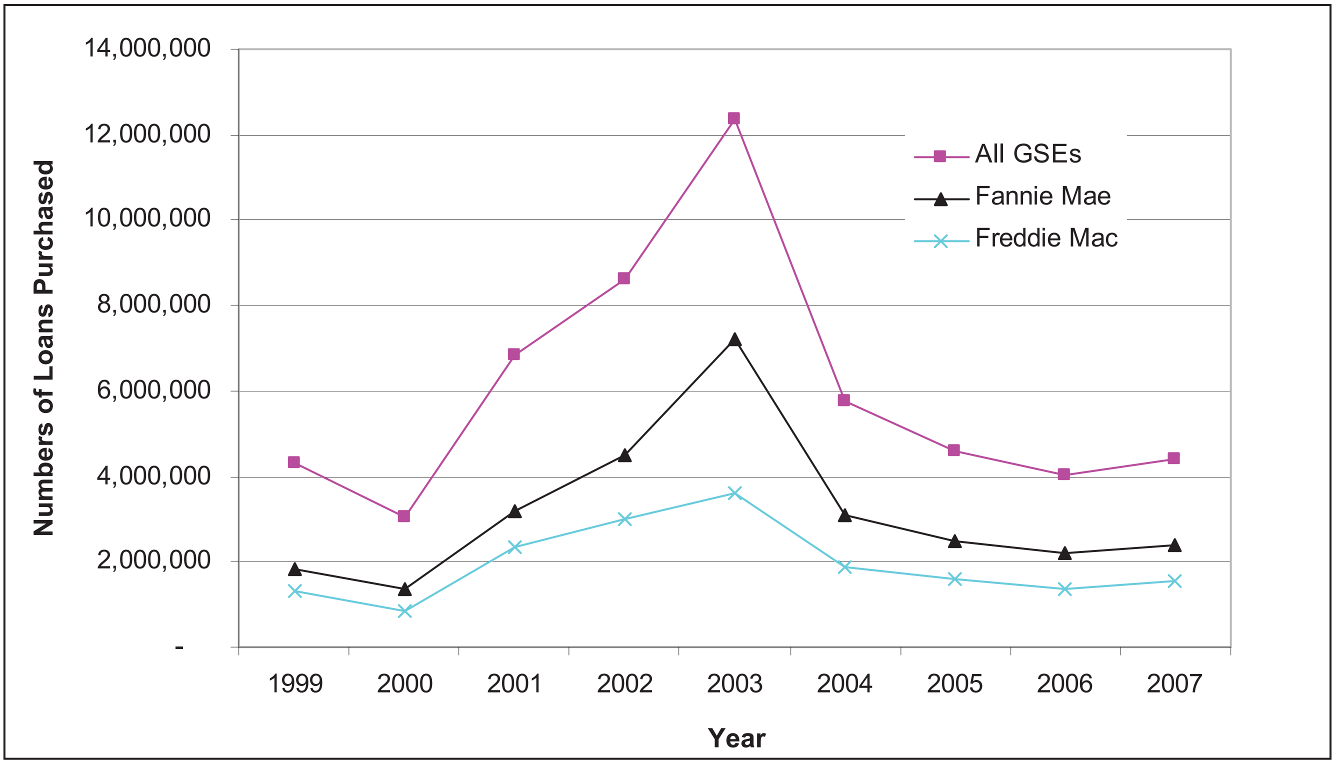
Caption: The numbers of GSEs’ purchased loans to White borrowers from1999 to 2007 far exceed those to minority borrowers. These numbers show a dramatic increase, in millions of mortgages (e.g., from 2 to 8 million for all GSEs), from 2000 to 2003, and then decline (to less than 3 million) in 2006, with a slight increase in 2007. Both Fannie Mae and Freddie Mac show similar patterns. Compared to the scale of GSEs’ purchased loans to White borrowers, those involving minorities’ mortgages appear flat from 1999 to 2007.

C. GSEs’ Share of the Lending Market Over Time

Figure 3.32 shows the total number of loans GSEs purchased from 1999 to 2007. In 1999, all four GSEs purchased a total of 4,294,620 loans. The number then dropped to just over 3 million in 2000 before growing more than fourfold during the next three years, reaching a total of 12,241,973 in 2003. It then dropped drastically to below 6 million in 2004 and just over 4 million in 2006. The number of loans all GSEs purchased grew slightly in 2007, reaching a total 4,410,553.

Fannie Mae and Freddie Mac followed this same pattern of growth and decline in loan purchases. Fannie Mae purchased 1,815,193 loans in 1999, then only 1,361,352 loans in 2000. Growing thereafter, it purchased more than five times as many loans —7,219,289—in 2003. After the reductions in ensuing years, it purchased only 2,212,837 loans in 2006 and slightly more—2,406,229—in 2007. Freddie Mac purchased 1,331,081 loans in 1999, but only 838,712 loans in 2000. It increased the number of loans purchased to 3,601,946 in 2003, then declined to 1,359,056 loans in 2006. In 2007, it purchased 1,532,893 loans.

Figure 3.32
Counts of GSEs' Loans Purchased (of Financial Institutions' Originations and Purchased Loans), 1999–2007



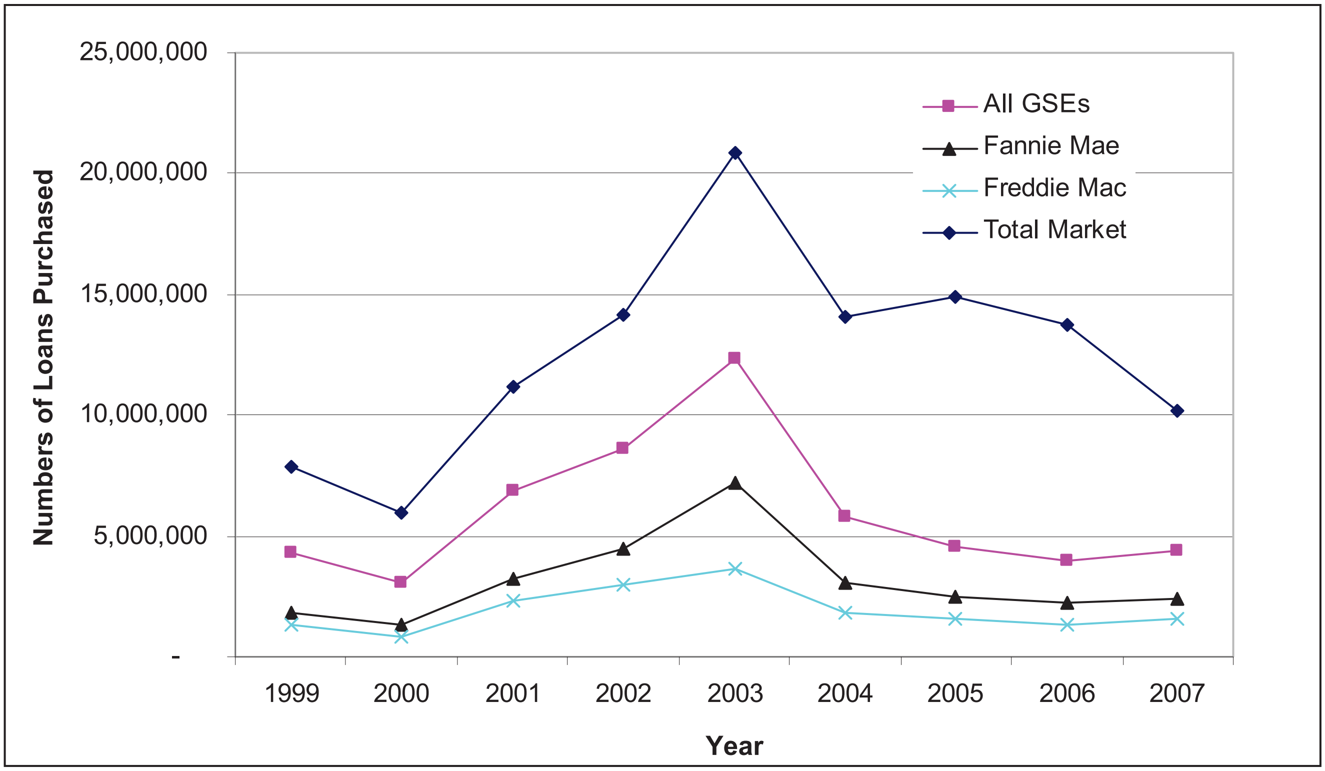
Note: The category "All GSEs" includes Fannie Mae, Freddie Mac, Ginnie Mae, and Farmer Mac.

Source: Compiled by the U.S. Commission on Civil Rights using HMDA data, tables 3 or 3.1 for 1999 to 2007.

Caption: Counts of loans GSEs purchased decreased slightly from 1999 to 2000, then increased steadily from 2000 to 2003, from around 3 million to over 12 million. From 2003 to 2004 the number of loans GSEs purchased dropped drastically, from over 12 million to under 6 million, and the downward trend continued through 2006, with only a slight increase in 2007. Fannie Mae and Freddie Mac followed similar trends, with Fannie Mae's purchased loans peaking at over 7 million in 2003, Freddie Mac's reaching less than 4 million then, and both having purchased roughly 2 million in 2007.

As reflected in Figure 3.33 up through 2007, the total market of loans reported in HMDA data mirrored that of the GSEs, but not thereafter. Whereas the GSEs experienced a sharp drop in the number of loans purchased in 2004, and continued to decline, the market measured as a whole remained relatively stable in 2005 and 2006, before declining severely in 2007. This would seem to indicate that the GSEs' share of the overall market was declining during this period.

Figure 3.33
The Number of Loans Purchased (of Financial Institutions' Originations and Purchased Loans), 1999–2007



Note: The category "All GSEs" includes Fannie Mae, Freddie Mac, Ginnie Mae, and Farmer Mac. The "Total Market" is all loans reported in HMDA data. The legend of figure 3.35 lists the other types of purchasers in this "market."

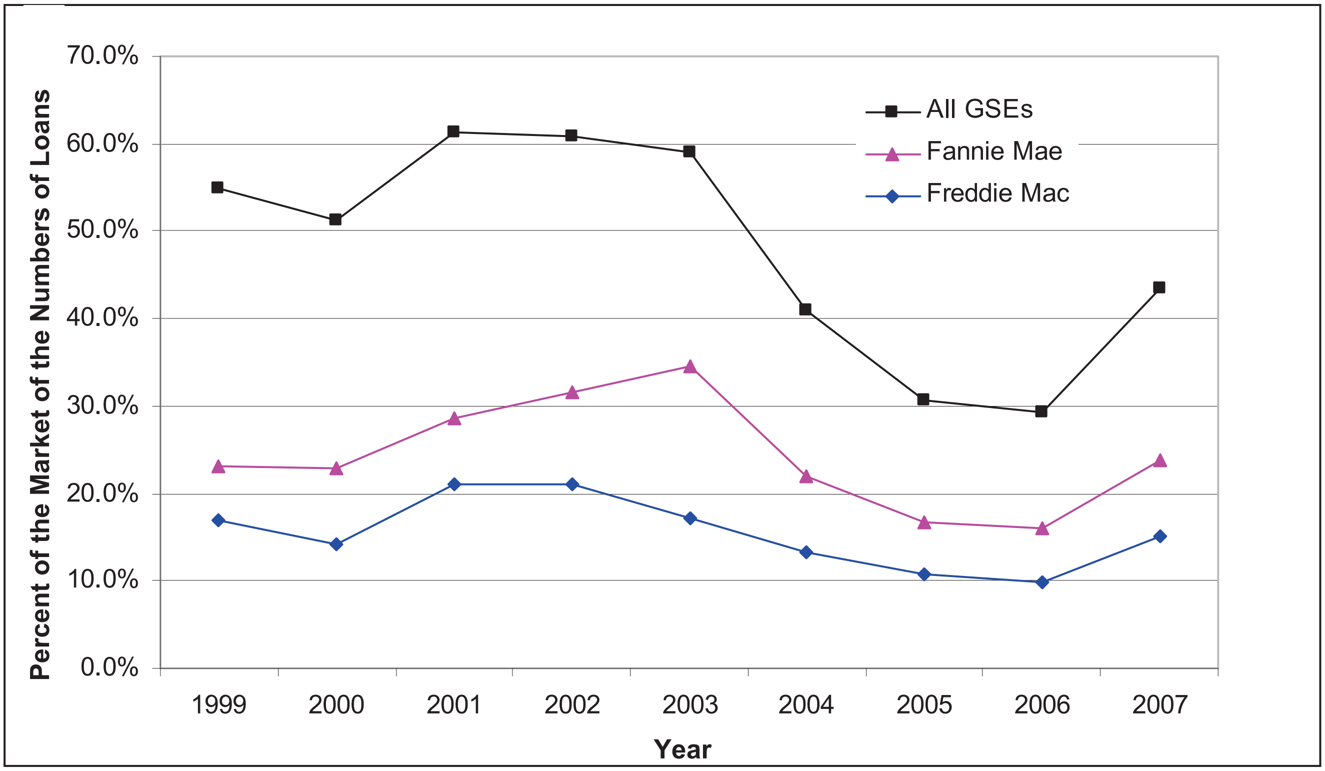
Source: Compiled by the U.S. Commission on Civil Rights using HMDA data, tables 3 or 3.1 for 1999 to 2007.

Caption: Comparing the numbers of GSEs' purchased loans to those of the other financial institutions that bought loans reported in HMDA data, the GSEs and the whole market followed similar trends through 2004. Notably the HMDA data show purchases of more than 20 million loans in 2003, but less than 15 million in 2004. But HMDA data also show sustained numbers of purchased loans during 2004 to 2006, whereas those that the GSEs bought dwindled.

While Figure 3.33 looked at the number of loans generated, Figure 3.34 shows the percentage share of the market that GSEs' loan purchases represented. Notably, GSEs purchased 54.9 percent of loans in HMDA-covered loans in 1999 and 51.2 percent in 2000. Their share then rose to 61.2 percent in 2001 and remained near 60 percent through 2003. It then plunged to less than half that amount—29.2 percent—by 2006. In 2007 the GSEs' share (of a declining market) increased to 43.4 percent.

Figure 3.34 indicates that Fannie Mae and Freddie Mac followed a pattern generally similar to GSEs as a whole, differing only in the years of their peak and the start of the decline. Fannie Mae's purchased loans comprised approximately 23 percent of the market in 1999 and 2000, rose to 34.5 percent in 2003, then declined to 16.1 percent in 2006 and increased to 23.7 percent in 2007. Freddie Mac purchased 17 percent of the loans reported in HMDA data in 1999, 14.1 percent in 2000, then 21 percent in 2001 and 2002. It declined thereafter to 9.9 percent in 2006, but grew to 15.1 percent in 2007.

Figure 3.34
GSEs' Purchased Loans' (of Financial Institutions' Originations and Purchased Loans) Percent of the Market, 1999–2007



Note: The "market" represents the totality of loans reported in HMDA data. The category "All GSEs" includes Fannie Mae, Freddie Mac, Ginnie Mae, and Farmer Mac.

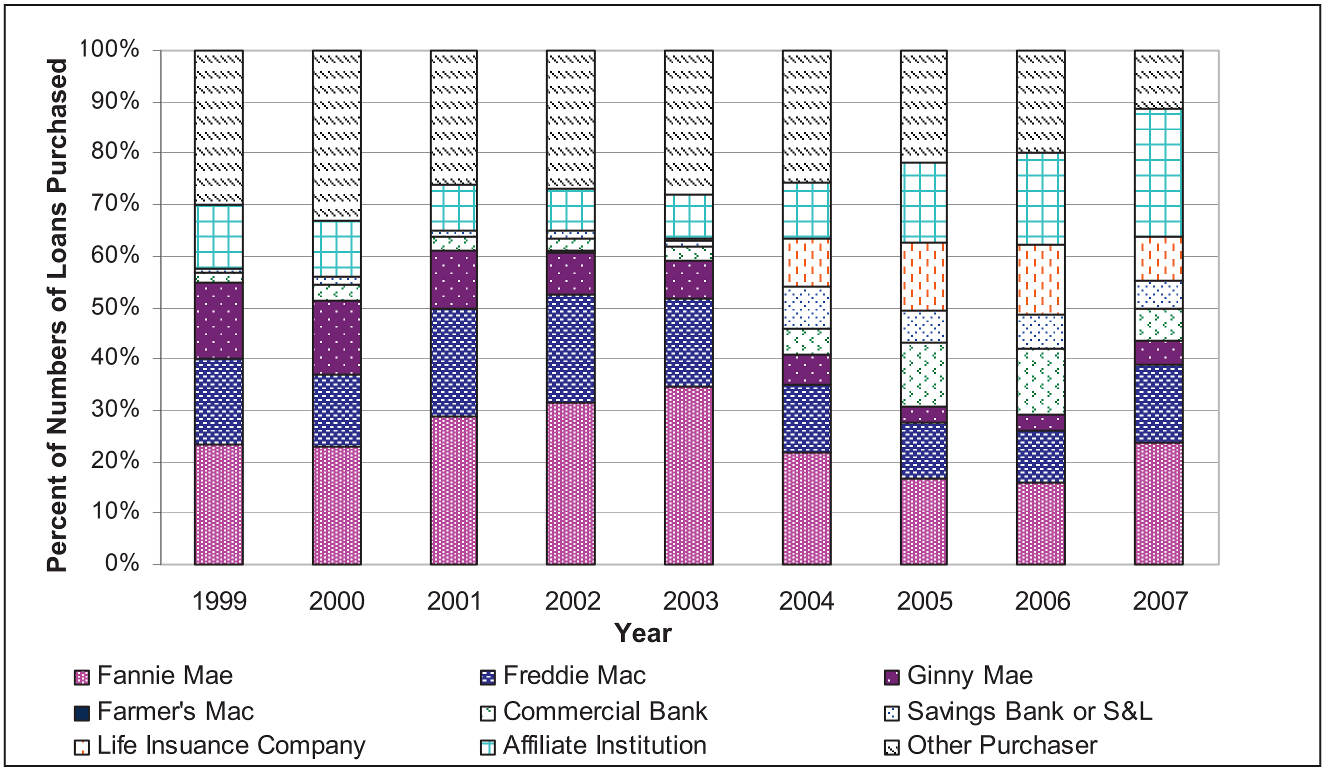
Source: Compiled by the U.S. Commission on Civil Rights HMDA data, tables 3 or 3.1 for 1999 to 2007.

Caption: In 1999, GSE-purchased loans made up about 55 percent of the market of HMDA-reported loans, then fell to just over 50 percent in 2000. From 2001 to 2003 the loans GSEs purchased comprised about 60 percent of the market, but decreased beginning in 2003, reaching a mere 30 percent in 2005 to 2006, and then rose to around 45 percent in 2007. Fannie Mae and Freddie Mac's percentage of the market followed similar trends, with Fannie Mae's market share ranging from near 15 to 35 percent and Freddie Mac's from about 10 to 21 percent during 1999 through 2007.

The GSEs' and other financial institutions' loan purchases, as a share of the total market of loans reported in HMDA data, are shown in greater detail in Figure 3.35. The 1999 to 2007 trend lines for Fannie Mae and the combined GSEs match those appearing in Figure 3.34. Notably, only three of the GSEs—Fannie Mae, Freddie Mac, and Ginnie Mae—are visible in the chart because the market share of Farmer Mac was essentially zero percent in all years.

Figure 3.35 reflects that the GSEs' share of the market of HMDA-reported loans decreased significantly between 2003 and 2004, as more of this market was taken over by non-governmental competitors of the GSEs.

Figure 3.35
Percent of the Number of Loans by Type of Purchaser (Originations and Purchased Loans), 1999–2007



Source: Compiled by the U.S. Commission on Civil Rights using HMDA data, tables 3 or 3.1 for 1999 to 2007.

Caption: As the GSEs' (i.e., Fannie Mae's, Freddie Mac's, Ginnie Mae's, and Farmer Mac's) share of purchased HMDA-reported loans dropped from 50 to 60 percent in 1999 to 2003 to 30 to 45 percent in 2004 to 2007, the proportion of HMDA loans other types of financial institutions purchased increased. Notably, Life Insurance Companies, Savings Bank or S&Ls, Commercial Banks, and Affiliate Institutions purchased much larger proportions of HMDA-reported loans in 2004 to 2007 than they had in 1999 in 2003.

In sum, the GSEs' growth mirrored the growth in homeownership from 2000 to 2004. Thereafter, however, the GSEs' share of the market experienced a substantial drop. As far as minority lending, both the number and monetary volume of loans purchased by the GSEs from minorities mirrored the overall growth of homeownership. At all stages, however, the overwhelming majority of loans purchased by the GSEs were to Whites.

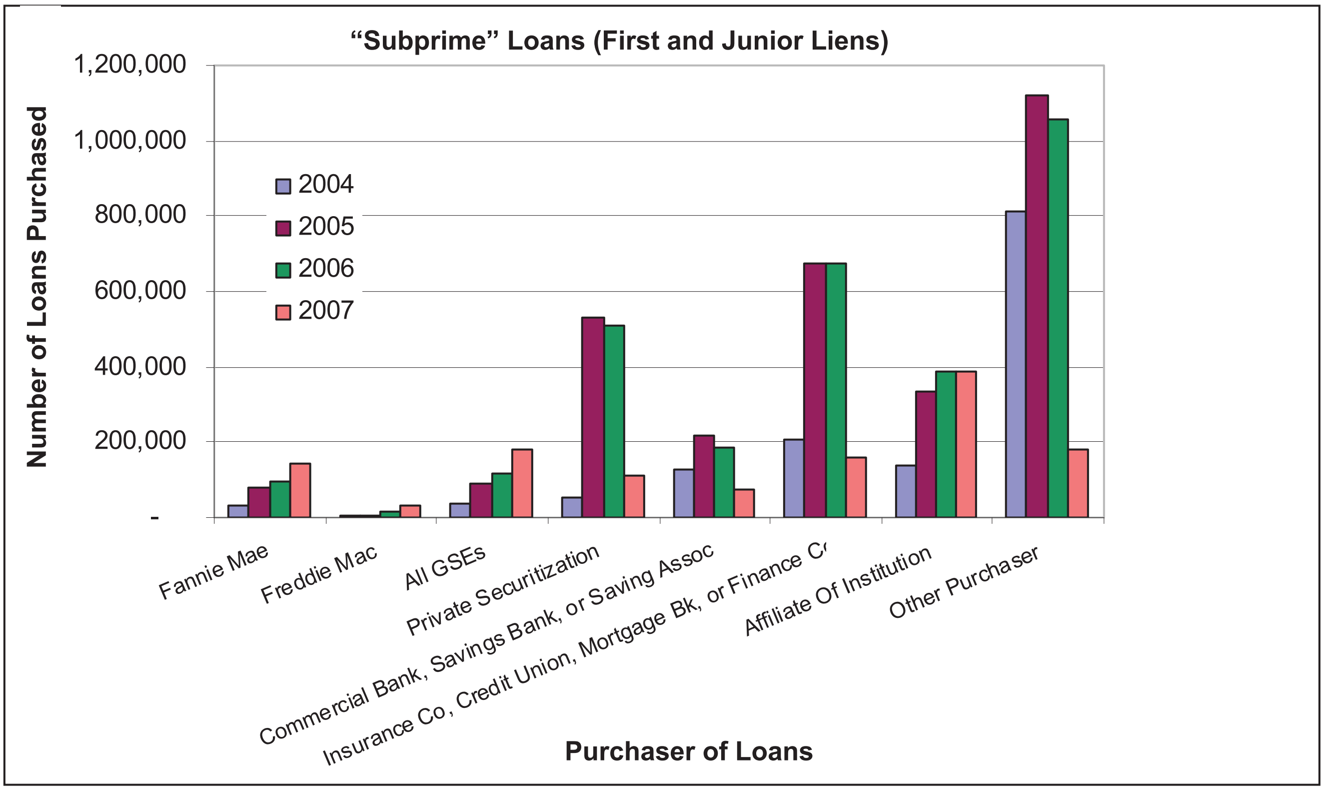
D. GSEs' Volume of Purchasing Subprime Lending Over Time

As discussed in Chapter 2, it has been contended that the HUD lending goals contributed to the increase in subprime lending. This next section examines data relating to this claim. As discussed in more detail herein, the data reflect that, while the purchase of subprime mortgages by the GSEs increased from 2004 through 2007, other players in the market captured substantially larger portions of this market.

At the same time, the data reflect that the GSEs continued their purchase of subprime loans after other purchasers began leaving the market. These purchases by the GSEs were often in the form of private label securities.

Unlike Figures 3.32 through 3.35, which included originations and purchases, the loans in Figures 3.36 through 3.39 (that relate to loan pricing on prime vs. subprime loans) contain originations only. Because of the costs lenders incur in complying with reporting and disclosure requirements, in 2002, when the Federal Reserve Board revised Regulation C, it limited the scope of its application to the disclosure of pricing on loan originations. Thus, any indication of pricing is lacking in HMDA data for mortgages purchased from other entities or applications that did not result in a loan origination.[49]

Figure 3.36
Number of Subprime (Higher-Priced) Loans (Both First and Junior Liens) (Originations Only) By Type of Purchaser, 2004–2007



Note: The category "All GSEs" includes Fannie Mae, Freddie Mac, Ginnie Mae, and Farmer Mac.

---

[49] Robert B. Avery and Glenn B. Canner, both of the Division of Research and Statistics, and Robert E. Cook, of the Division of Consumer and Community Affairs, Federal Reserve Board, *New Information Reported under HMDA and Its Application in Fair Lending Enforcement*, FED. RES. BULL., December 2008, p. 349. The guide for reporting HMDA data instructs financial institutions to report pricing information "[f]or a home purchase loan, a refinancing, or a dwelling-secured home improvement loan that you originated," and to enter "nonapplicable" "[i]f the loan is not subject to Regulation Z, or is a home improvement loan that is not dwelling-secured, or is a loan that you purchased," or "in the case of an application that does not result in a loan origination. Federal Financial Institutions Examination Council, *A Guide to HMDA Reporting: Getting It Right*, at pp. A–8 to –9.

Source: Compiled by U.S. Commission on Civil Rights using HMDA data, table 3.2 for 2004 to 2007.

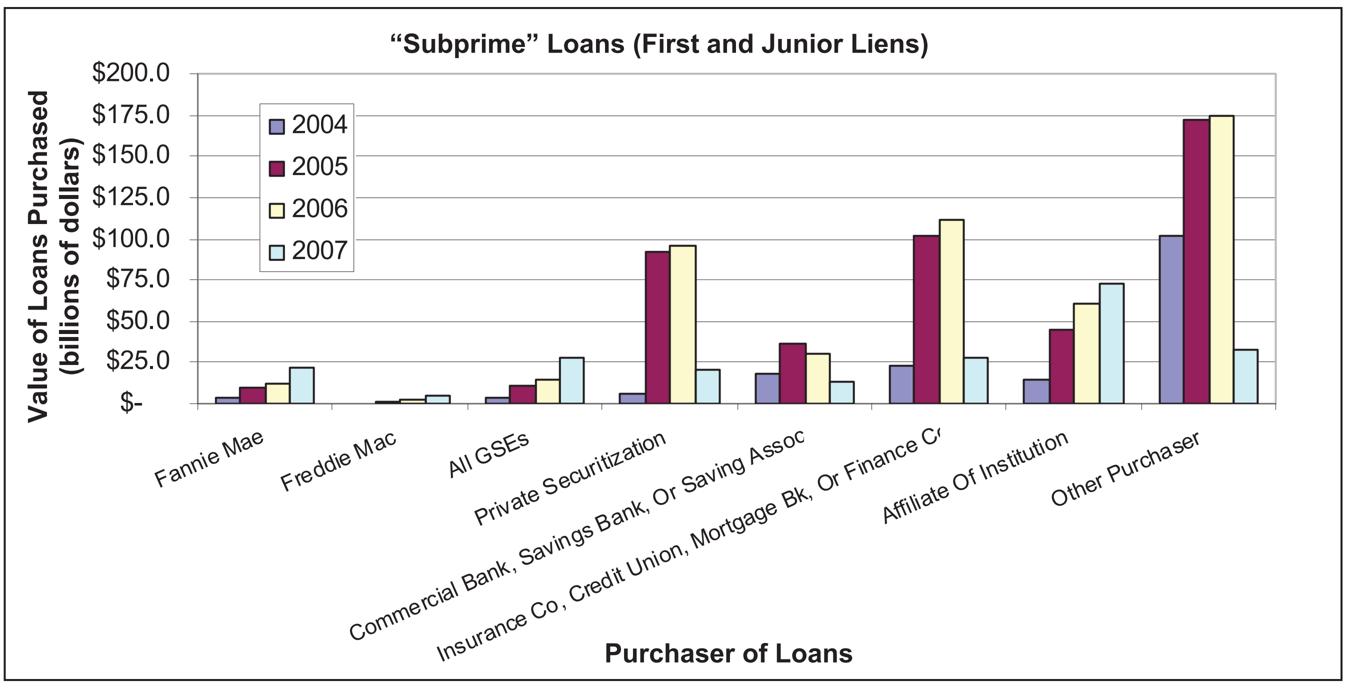
Caption: From 2004 to 2007, Fannie Mae and Freddie Mac increased the number of subprime (i.e., higher-priced) loans they purchased each year. However, at less than 200,000, the number of loans that all four GSEs purchased in 2007 made up a very small amount of the market of HMDA-reported, higher-priced loans. Other types of financial institutions, for example, insurance companies, credit unions, mortgage banks, or finance companies, purchased higher-priced loans in far greater numbers than the GSEs, particularly in 2005 and 2006. However, the volume of these non-government enterprises' purchases were more in line with the GSEs' in 2007.

Figures 3.36 and 3.37 show that the GSEs purchased only a very small proportion of the subprime originations from those financial institutions under federal regulation or otherwise required to report HMDA data. Figure 3.36 examines the number of subprime loans purchased. It indicates that the GSEs' share of said market was minimal compared to others.

Figure 3.37 examines the value of purchased subprime loans. Again, the GSEs' share of said market was overwhelmed by other purchasers.

Both with regard to number and value of loans, it is notable that, while the GSEs were never major purchasers of subprime loans, their share of the market did increase in 2007, at a time when other purchasers began to exit the market.

Figure 3.37
Value of Subprime (Higher-Priced) Loans (Both First and Junior Liens) (Originations Only) By Type of Purchaser, 2004–2007



Note: The category "All GSEs" includes Fannie Mae, Freddie Mac, Ginnie Mae, and Farmer Mac.

Source: Compiled by the U.S. Commission on Civil Rights using HMDA data, table 3.2 for 2004 to 2007.

Caption: By dollar value, the GSEs' share of purchases of higher-priced loans is dwarfed by the purchases of other types of financial institutions in 2005 and 2006. The maximum value of GSEs' purchases of higher-priced loans reached $25 billion in 2007, and other types of purchasers bought similar amounts that year. However, earlier, in 2005 and 2006, three other types of purchasers (as identified in HMDA data) bought $100 to $175 billion each.

E. Fannie Mae and Freddie Mac's Purchasing of Private-Label Securities Over Time

Figure 3.38 shows the purchases Fannie Mae and Freddie Mac made of private-label mortgage-related securities. The total includes single-family loans as well as multifamily and manufactured housing mortgages.

Prior to 1995, Fannie Mae had not purchased any private-label mortgage-related securities. Beginning in 1995 and 1996, it purchased only small amounts—$752 million and $777 million, respectively. It increased its purchases to $4.2 billion in 1997, then $15.7 in 1998, and $16.5 billion in 1999. It reduced its purchases to amounts ranging between $3.5 and $8.5 billion in 2000 through 2002. Then, in 2003, it doubled the amount of any previous year's purchases to $34.0 billion, and more than doubled that amount again—to $90.7 billion—in 2004. Since then, Fannie Mae's purchased amounts were less than that of 2004, but still more than that of 2003—$41.4, $57.8, and $37.4 billion in 2005 to 2007, respectively.

Information on Freddie Mac's purchases of private-label mortgage-related securities prior to 1997 is unavailable. In 1997, Freddie purchased $1.5 billion such securities. In 1998 and 1999, it purchased $15.7 and $15.2 billion. In 2000 it bought $10.3 billion worth of securities. In 2001 through 2003, it purchased $24.5, $59.4, and $69.2 billion respectively. In 2004, its purchases almost doubled to $121 billion and increased yet again in 2005 to $180 billion. By 2006 the amount declined to $122 billion, before undergoing a drastic reduction to $76.1 billion in 2007.

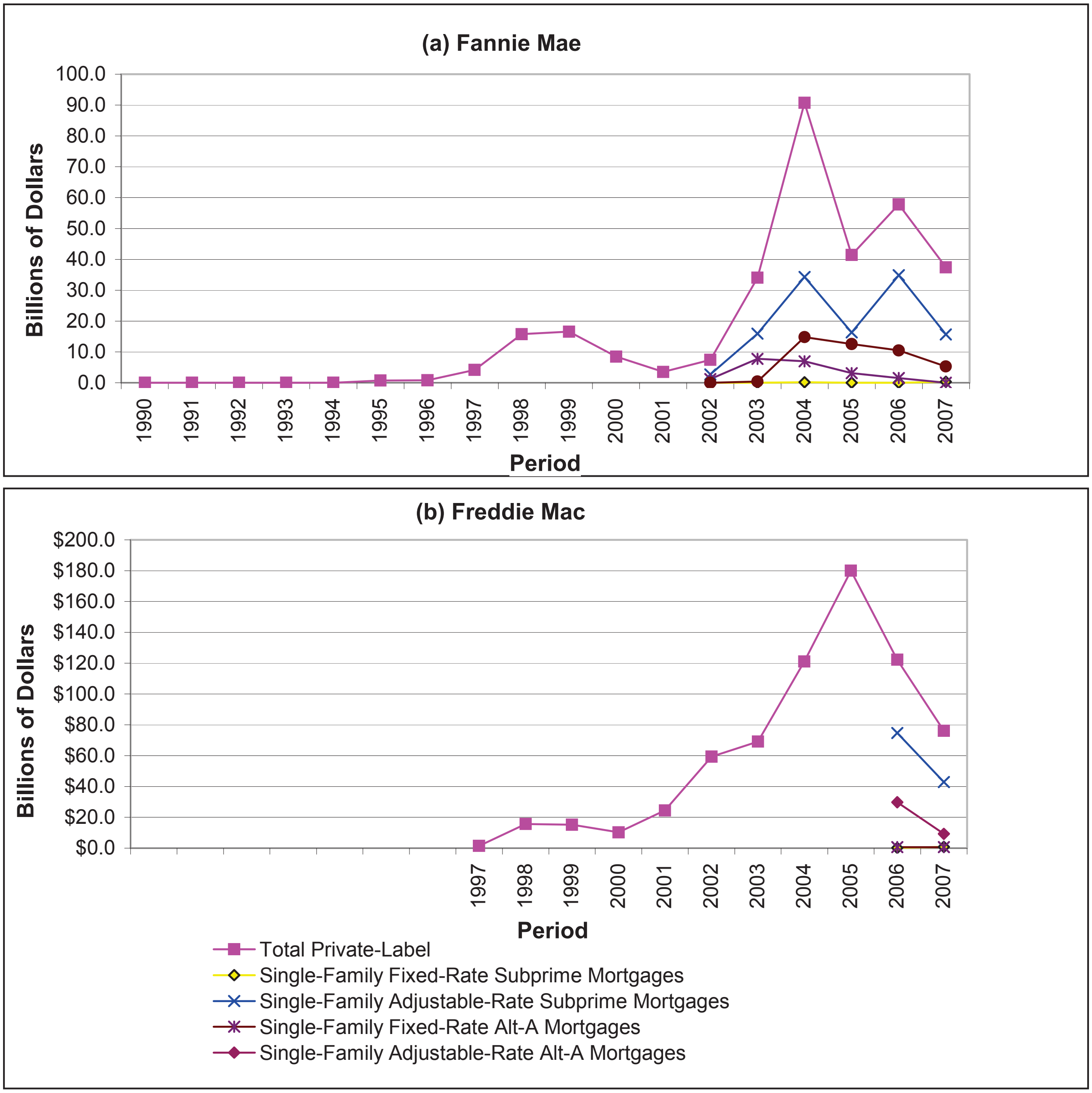
Detailed information on the types of private-label mortgage-related securities Fannie Mae and Freddie Mac purchased is only available for the former for 2002 to 2007 and the latter in 2006 and 2007. Figure 3.39 shows the amounts of single-family fixed- and adjustable-rate subprime and Alt-A mortgages that the two GSEs purchased for these years.

As shown in Figure 3.38, fixed-rate securities backed by single-family subprime mortgages were never a large part of the private-label securities Fannie Mae and Freddie Mac purchased.[50] They amounted to $176 and $343 million of Fannie Mae's purchases in 2004 and 2007 respectively, and $116 and $843 million of Freddie Mac's in 2006 and 2007. These small amounts are not visibly different from zero on the scale of overall private-label mortgage-related securities the GSEs purchased as shown in Figure 3.38. The 2007 amounts comprised about 1 percent of each GSE's total purchases of private-label mortgage-related securities.

---

[50] Office of Federal Housing Enterprise Oversight, *Mortgage Markets and the Enterprises in 2007*, July 2008, p. 56 table 1b part 2, p. 73 table 10b part 2. Note that in many instances adjustable rate securities that Freddie Mac or Fannie Mae purchased might include fixed rate, adjustable rate or both types of mortgage loans as the underlying collateral backing such securities. One should not assume that all loans backing adjustable rate securities are adjustable rate mortgages. Letter from Alfred M. Pollard, general counsel, Federal Housing Finance Agency, to David Blackwood, general counsel, U.S. Commission on Civil Rights, July 15, 2009, attachment, p. 4.

Figure 3.38
Fannie Mae and Freddie Mac Purchases of Private-Label Mortgage-Related Securities, 1990–2007



Notes: In addition to single-family subprime and Alt-A mortgages, the total private-label securities include other single-family loans, as well as multifamily and manufactured housing mortgages. The amounts of the purchases are based on unpaid principal balances and exclude mortgage-related securities that were traded, but not yet settled. Also, for Freddie Mac, data on the total private-label securities were unavailable prior to 1997. In addition, for the period 2001 through 2003, the data are based on restated financial results. Prior to 2006, the total represents, in part, "other" single-family loans that include non-Freddie Mac mortgage-related securities purchased for structured securities as well as non-agency securities purchased into the retained mortgage portfolio (principally backed by subprime or Alt-A loans).

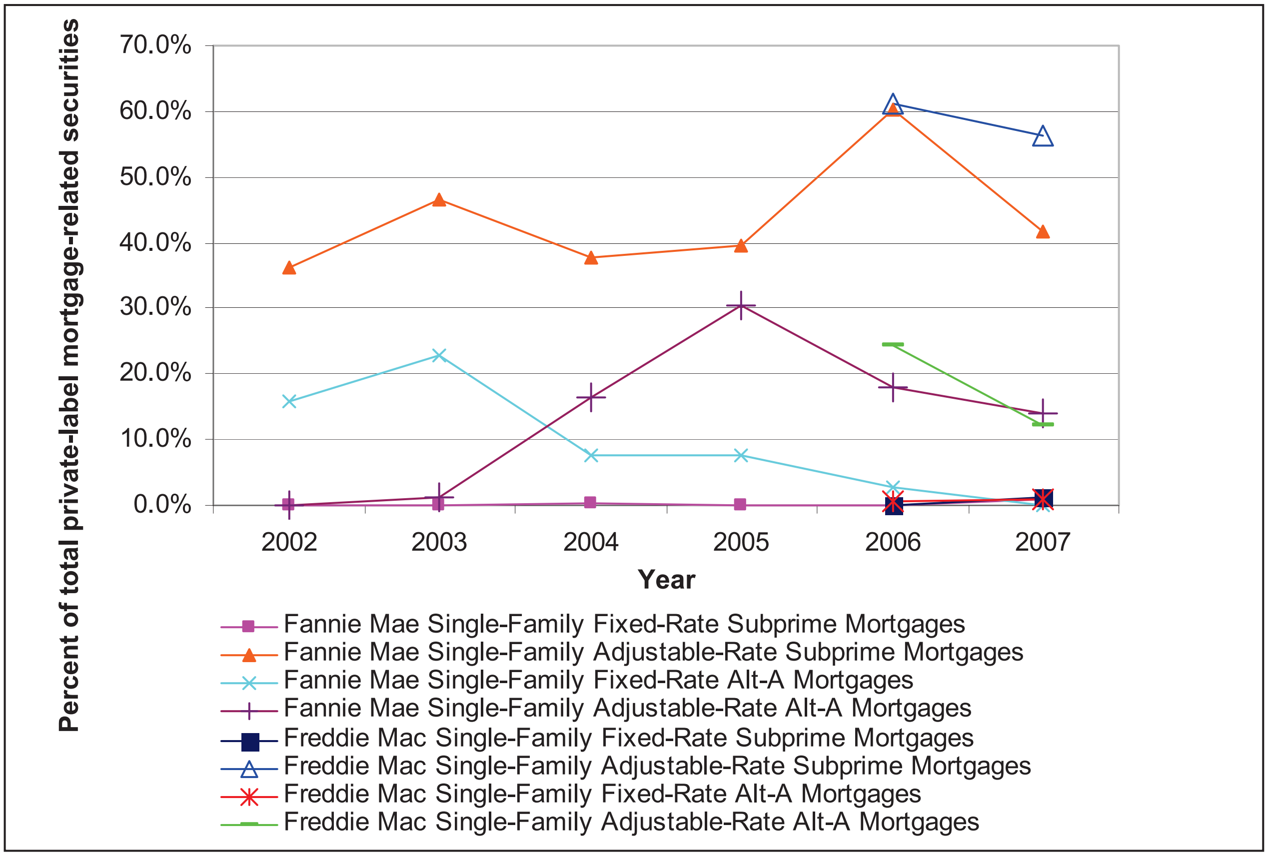
Source: Office of Federal Housing Enterprise Oversight, *Mortgage Markets and the Enterprises in 2007*, July 2008, p. 56 table 1b part 2 (citing Fannie Mae), p. 73 table 10b part 2 (citing Freddie Mac), *available at* <http://www.ofheo.gov/media/research/MME2007.pdf> (last accessed Apr. 27, 2009).

Caption: Both Fannie Mae and Freddie Mac greatly increased their purchases of private-label mortgage-related securities from 2001 to 2005, going from around $5 to $90 billion in the case of Fannie Mae, and from over $20 to $180 billion for Freddie Mac. Their purchases decreased from 2005 to 2007 but still remained well above their pre-2001 level, with Fannie Mae falling to about $40 billion in 2007, Freddie Mac to $80 billion. Among the private label securities, Fannie Mae's purchases of single-family adjustable-rate subprime mortgages fluctuated between $15 and$35 billion in 2003 to 2007. The value of Freddie Mac's single-family adjustable-rate mortgages is only available for two years and fell from below $80 billion in 2006 to just over $40 billion in 2007.

As to single-family adjustable-rate subprime mortgages, Fannie Mae only purchased $2.7 billion such private-label securities in 2002. Thereafter, however, the amount was much larger, fluctuating between $15.6 and $34.9 billion. *See* Figure 3.38. Freddie Mac purchased $74.6 billion in single-family adjustable-rate subprime mortgages among private-label securities in 2006 and $42.8 billion in 2007. Furthermore, single-family adjustable-rate subprime mortgages comprised a major part of the GSEs' private-label mortgage-related securities.

Figure 3.39 shows that for Fannie Mae these were 36 percent of the GSE's private-label purchases in 2002, 47 percent in 2003, 38 percent in 2004, and 40 percent in 2005. In 2006 they were 60 percent of the private-label purchases, but the proportion fell to 42 percent in 2007. Freddie Mac purchases of single-family adjustable-rate subprime mortgages were a similarly large proportion of its private-label securities in 2006—61 percent—and only a slightly smaller proportion—56 percent—in 2007.

Figure 3.39
Proportion of Fannie Mae's and Freddie Mac's Purchases of Private-Label Mortgage-Related Securities that Were Single-Family Subprime or Alt-A, 2002–2007



Notes: In addition to single-family subprime and Alt-A mortgages, the total private-label securities include other single-family loans, as well as multifamily and manufactured housing mortgages. Information on subprime and Alt-A mortgages was unavailable before 2002 for Fannie Mae and before 2006 for Freddie Mac.

Source: Compiled by the U.S. Commission on Civil Rights using Office of Federal Housing Enterprise Oversight, *Mortgage Markets and the Enterprises in 2007*, July 2008, p. 56 table 1b part 2 (citing Fannie Mae) p. 73 table 10b part 2 (citing Freddie Mac).

Caption: Fannie Mae's purchases of single-family adjustable-rate subprime mortgages were 35 to 45 percent of total private-label mortgage-related securities in 2002 to 2004, then rose to 60 percent in 2006 and fell back to just over 40 percent in 2007. Fannie Mae's single-family fixed-rate Alt-A mortgages declined over the time period, from over 20 percent in 2003, to nearly 0 percent in 2006 and 2007. In contrast, Fannie Mae single-family adjustable-rate Alt-A mortgages increased from 0 to 30 percent from 2003 to 2005, then decreased from 30 to 15 percent over the course of 2005-2007. The similar proportion of Freddie Mac's purchases is only available for 2006 and 2007.

During 2002 to 2007, Fannie Mae began purchasing more Alt-A adjustable-rate, and less Alt-A fixed-rate, mortgages. Figure 3.39 indicates that, in 2002, the private-label securities that Fannie Mae purchased included $1.2 billion in single-family fixed-rate Alt-A loans. This amount rose to $7.7 billion in 2003 and then diminished to $7.0 billion in 2004, $3.1 billion in 2005, $1.5 billion in 2006, and, finally, a mere $38 million in 2007.

The extent of Freddie Mac's purchases of single-family Alt-A loans is known only for 2006 and 2007. It purchased relatively small amounts of single-family Alt-A fixed rate mortgages—$718 million in 2006 and $702 million in 2007—but large numbers of single-family Alt-A adjustable-rate loans—$29.8 billion in 2006 and $9.3 billion in 2007.

The proportion of Fannie Mae's purchases of private-label mortgage-related securities that were single-family fixed- and adjustable-rate Alt-A loans reflects that Fannie Mae and Freddie Mac made a shift from buying fixed-rate loans, to purchasing variable-rate loans. *See* Figure 3.39. Thus, purchases of such fixed-rate mortgages represented 15.7 percent of private-label securities for Fannie Mae in 2002 and 22.7 percent in 2003. In 2004 and 2005, the percentage dropped to 7.7 and 7.5 percent. In 2006, only 2.6 percent were single-family fixed-rate Alt-A loans, and, in 2007, only a small fraction of a percent (0.1%) were.

Looking at adjustable-rate mortgages for Alt-A loans, beginning from nothing in 2002, Fannie Mae increased the percentage that single-family, adjustable rate Alt-A loans represents of its private-label loans to 1.1 percent in 2003, then 16.3 percent in 2004, and 30.3 percent in 2005. In 2006 and 2007, the percentage decreased to 18.1 percent in the former year and 14.0 percent in the latter. Freddie Mac's purchases as reported and shown in Figure 3.39 indicate that single-family Alt-A fixed-rate loans represented less than one percent of this GSE's private-label purchases (i.e., 0.6 and 0.9 percent) in 2006 and 2007, while single-family adjustable-rate mortgages are 24.4 percent and 12.2 of its 2006 and 2007 private-label purchases.

The above data are useful in addressing the arguments raised in Chapter 2 of this section. For purposes of analysis, the salient points have been broken down to four categories, set forth below.

General Housing Information

- During the period from 1994 through 2005, overall ownership rates increased for each of the ethnic and/or racial subgroups examined. During this period, each minority racial or ethnic group showed stronger rates of growth than Whites.
- Even following the collapse of the housing bubble, racial and ethnic minority groups still showed stronger rates of growth than Whites.
- Despite the growth of minority homeownership, and the narrowing of the gap between various groups, substantial racial and ethnic disparities in homeownership rates remain. In 2008, the White homeownership rate stood at 71.7 percent, that of Asian/Pacific Islanders at 59.5 percent, American Indians at 56.5 percent, Hispanics at 49.1 percent, and Blacks at 47.4 percent.
- As to conventional loans, minorities experienced both the greatest percentage of growth as the market expanded as well as the greatest percentage of decrease as the market began to tighten.
- When credit history was taken into consideration, the denial rate of Whites and Blacks regarding conventional mortgage applications narrowed. The gap between the denial rates of Whites and Blacks regarding refinance loans, however, did not close significantly over time.

Subprime Mortgages

- The percentage of subprime conventional and refinance mortgages given to all racial and ethnic groups followed roughly the same pattern, increasing dramatically between 2004 and 2005, remaining high in 2006, and dramatically decreasing between 2006 and 2007. For most minority groups, however, the percentage receiving such loans was higher than for Whites.
- While foreclosure rates have increased for all classes of loans, the highest rate of foreclosure is attributable to subprime adjustable rate mortgages. The next highest rate of foreclosure was amongst subprime fixed-rate mortgages, followed by prime adjustable rate mortgages. Prime fixed-rate mortgages have the lowest rate of foreclosure.
- From 2004 to 2007, the monetary volume of subprime loans to middle- and upper-income borrowers/neighborhoods consistently exceeded those made to lower- and moderate-income groups.
- Between 2004 and 2007, middle- and upper-income borrowers/neighborhoods were the largest consumers of subprime loans. This is so whether measured by number of loans or monetary value.
- Independent mortgage companies were most likely to make the highest percentage of both home purchase loans and refinance loans in minority neighborhoods, regardless of income level.

Community Reinvestment Act

- Between 1994 and 2005, mortgage lending within CRA assessment areas has suffered a steady rate of decline, with only a modest rise since that time. Whether measured by number or value of loans, the CRA share of the subprime market has been modest.
- Of subprime loans made by banking institutions and their affiliates, the smallest percentages were originated within an institution's CRA assessment area.
- The largest percent of subprime loans, by a substantial margin, were made by either independent mortgage companies or banking institutions outside their CRA assessment areas.
- The number of prime loans that banking institutions and their affiliates originated in low- and moderate-income borrowers/neighborhoods within their CRA assessment areas was consistently a very small portion of all prime loans originated.
- Irrespective of the racial composition and income level of neighborhoods, banking institutions and their affiliates were still less likely to make home purchase loans within their CRA assessment areas than outside them.
- In 2006, banking institutions and their affiliates were less likely to make loans within their CRA assessment areas, regardless of the race or ethnicity of borrowers, for either purchase or refinance loans.

Fannie Mae/Freddie Mac/GSEs Generally

- From 1999 to 2007, and particularly from 2004 through 2007, Hispanics and Blacks received increasingly larger proportions of loans that Fannie Mae and Freddie Mac purchased. Nevertheless, the overwhelming majority of such loans involved White borrowers.
- The rise and decrease in purchases by GSEs roughly followed the same pattern for all racial and ethnic groups. The number of loans purchased by GSEs generally, and Fannie Mae and Freddie Mac in particular, increased greatly from 2000 through 2003. Such purchases decreased drastically after 2004, and slightly increased between 2006 and 2007.
- During the period from 2004 to 2007, Fannie Mae and Freddie Mac purchased only a very small portion of the subprime originations from financial institutions under federal regulation or otherwise required to report HMDA data. Both with regard to the number and value of such loans, the GSEs' share of the market increased in 2007, at a time when other purchasers began to exit the market.

The above data are inconclusive as to the extent to which either the CRA or the HUD lending goals contributed to the existing mortgage crisis. While both policies sought relaxed lending standards in an effort to increase homeownership, especially with regard to minorities, there is insufficient evidence to indicate to what degree the pressure for relaxed lending standards influenced the overall market. At all stages, third-party purchasers and those not governed by the CRA had substantially larger shares of the applicable subprime market. Moreover, the data demonstrate that the majority of subprime loans were received by middle- and upper-income borrowers/neighborhoods.

At the same time, the evidence collected in this report does not support the contention that minority racial or ethnic groups were systematically targeted by predatory lending schemes involving subprime loans. As noted above, the majority of subprime loans were received by upper- and middle-income individuals or families. Throughout the period of the mortgage boom and bust, the lending patterns of Whites and racial and ethnic minorities mirrored each other.

As to the performance of Fannie Mae and Freddie Mac, the data reflect that third-party purchasers had substantially larger shares of the subprime secondary market. What can be discerned is that, at a time when others in the secondary market were decreasing their share of subprime mortgages, Fannie Mae and Freddie Mac were actually increasing their purchases, presumably to reflect the political and market pressures these organizations were feeling as discussed in Chapter 2.

PART II: PREDATORY LENDING, MORTGAGE FRAUD, AND MORTGAGE LENDING DISCRIMINATION

CHAPTER 4: PREDATORY LENDING, MORTGAGE FRAUD, AND MORTGAGE LENDING DISCRIMINATION

As discussed in Chapter 1 of this report, the federal government adopted policies to affirmatively increase minority homeownership. Since adoption of these policies, it is clear minority homeownership has increased. At the same time, it is also clear both that, as the housing boom came to an end, minorities have experienced higher rates of foreclosure and that they received subprime loans at a higher rate than have Whites.

These consequences raise a question as to whether policies adopted to affirmatively increase minority housing (in conjunction with the market forces discussed in Chapter 1) were, in the end, counterproductive, either because they inadvertently lured the unprepared into homeownership and/or created an environment conducive to fraud. There is support for both propositions.

In a January 2009 article, Representative Barney Frank, the Chairman of the House Financial Services Committee, was quoted as follows:

> According to Frank, at the root of the real-estate crisis was a misguided notion that homeownership should be available to all people — what President Bush has called "the ownership society." "The 'I told you so' here is that homeownership is a nice thing but it is not suitable for everybody," Frank said at Boston College. "There are people in this society who don't have enough money to be homeowners, and there are people whose lives are not sufficiently integrated for them to take on the responsibility to be a homeowner. And we did too much pushing of people into inappropriate mortgages and into homeownership."[1]

Under this view, government policies led too many unprepared individuals to become homeowners:

> There were real gains during the Clinton years, as homeownership rose to 67.4 percent in 2000 from 64 percent in 1994. Hispanics and African-Americans were the biggest beneficiaries. But as the boom later gathered steam, and as the Bush administration continued the Clinton administration's push to amplify homeownership, some of those gains turned out to be built on sand.[2]

In commenting on this scenario, Henry G. Cisneros, the former Secretary of the Department of Housing and Urban Development during the Clinton administration, stated:

---

[1] Jeffrey Toobin, *Barney's Great Adventure*, NEW YORKER, Jan. 12, 2009, at p. 38.

[2] David Streitfeld and Gretchen Morgenson, *Building Flawed American Dreams*, N.Y. TIMES, Oct. 19, 2008, at A1.

> You think you have a finely tuned instrument that you can use to say: 'Stop! We're at 69 percent homeownership. We should not go further. There are people who should remain renters,' … But you really are just given a sledgehammer and an ax. They are blunt tools.[3]

Others, however, have argued that it was the nature of the housing bubble itself which gave rise to an environment where fraud was possible and manipulation of the unsophisticated became inevitable.

> The short version of how we got here: Lenders, fat with money made cheap by the federal government, aggressively coaxed millions of borrowers to take out unaffordable mortgages. They lent this money without assessing whether borrowers could repay it. They assumed, in fact, that most wouldn't be able to and would have to refinance into new, equally unaffordable loans. This process would produce an endless cycle of fees for the lenders – but only if home prices rose, fairy-tale-like, forever.[4]

The above interpretation, however, fails to give consideration to the fact that the rapid appreciation in housing created a bubble that encouraged *all* parties to manipulate the system.[5] This process has been noted as follows:

> Throughout history, bubbles have induced fraud: "The propensity to swindle grows parallel with the propensity to speculate during a boom," wrote the eminent economic historian Charles Kindleberger. The implosion of an asset price bubble always leads to the discovery of frauds and swindles," he added. Said Bagehot, "The good times of too high price almost always engender much fraud."
>
> Our most recent bubble was no different. Some borrowers lied about their income to get loans; some mortgage brokers misled borrowers or falsified documents; and there were various schemes to defraud lenders. The euphoria about rising prices characteristic of bubbles also induces carelessness, which makes fraud easier.[6]

---

[3] *Id.*

[4] *See* Kathleen Day, *Villains in the Mortgage Mess? Start at Wall Street. Keep Going.*, WASH. POST, June 1, 2008, at B01.

[5] This problem was recognized by Rep. Barney Frank, Chairman of the House Financial Services Committee, in a recent interview:

> Question: Is the current mess a result of naïve consumers being duped into horrible mortgages, or is it a case of greedy consumers chasing cheap loans?
>
> Answer: Some where misled, others took part in the deception. There were people, for instance, who lied about their incomes. But we have made a mistake in this society. The assumption that everybody can be a homeowner is wrong. We pushed and encouraged people into homeownership — people who, in some cases, weren't ready for it. You can't act on wishes that are unrealistic without having negative consequences.

Janice Revell, CNN Money, *Housing: Frank talk from Barney Frank*, Aug. 25, 2008, <http://money.cnn.com/2008/08/22/real_estate/barney_frank.moneymag/index.htm?postversion=20080825107> (last accessed July 21, 2009).

[6] *See* Alex J. Pollock, *Your Guide to the Housing Crisis*, THE AMERICAN: THE JOURNAL OF THE AMERICAN ENTERPRISE INSTITUTE, May/June 2008, available at <http://www.american.com/archive/May-june-magazine-contents/your-guide-th-the-

As described more fully in Part I, the nature of the recent housing bubble sometimes created perverse incentives for both the lender and the borrower to commit fraud. The following incident is telling:

> As a supervisor at a Washington Mutual mortgage processing center, John D. Parsons was accustomed to seeing baby sitters claiming salaries worthy of college presidents, and schoolteachers with incomes rivaling stockbrokers'. He rarely questioned them. A real estate frenzy was under way and WaMu, as his bank was known, was all about saying yes.
>
> Yet even by WaMu's relaxed standards, one mortgage four years ago raised eyebrows. The borrower was claiming a six-figure income and an unusual profession: mariachi singer.
>
> Mr. Parsons could not verify the singer's income, so he had him photographed in front of his home dressed in his mariachi outfit. The photo went into a WaMu file. Approved.[7]

The data presented in Part I reflects that caution should be taken before jumping to simple conclusions. For example, while minorities may have taken out subprime loans at a higher rate than Whites, it is clear that Whites overall took out a majority of such loans. In addition, the evidence reflects that many subprime loans were taken out by high-income borrowers. The situation has been summarized as follows:

> While African Americans were more likely to be steered into subprime mortgages than white Americans, whites took out 56 percent of all subprime loans, far more than the 19 percent taken out by African Americans. The proportion was 21 percent for Hispanics. Money also increased the likelihood of a borrower taking out a subprime loan, but not in the way that conservatives claim. Most subprime loans went to high-income borrowers, according to data compiled as part of the 2006 Home Mortgage Disclosure Act. In fact, across all racial groups, as income decreased, the number of subprime loans decreased.[8]

The different motivations that guided borrowers and lenders, unfortunately, did not exclude racial discrimination. A June 2009 newspaper article discussing pending litigation involving the City of Baltimore reflected the following:

> As she describes it, Beth Jacobson and her fellow loan officers at Wells Fargo Bank "rode the stagecoach from Hell" for a decade, systematically singling out Blacks in Baltimore and suburban Maryland for high-interest subprime mortgages.

---

housing-crisis> (last accessed July 17, 2009); Peter S. Goodman and Gretchen Morgenson, *Saying Yes, WaMu Built Empire on Shaky Loans*, N.Y. TIMES, Dec. 28, 2008, at A1.

[7] *See also* CHARLES P. KINDLEBERGER, MANIAS, PANICS AND CRASHES: A HISTORY OF FINANCIAL CRISES 82 (1978) ("Greed not only creates suckers to be swindled by professionals but also pushes some of the amateurs over the line into fraud, embezzlement, defalcation, and similar misfeasance.").

[8] Tamara E. Holmes, *Did They Cause the Credit Crisis*, BLACK ENTERPRISE, Jan. 1, 2009, available at <http://www.blackenterprise.com/wealth-for-life/homeownership/2009/01/01/did-they-cause-the-credit-crisis-2> (last accessed July 21, 2009).

* * *

> Wells Fargo, Ms. Jacobson said in an interview, saw the black community as fertile ground for subprime mortgages, as working-class blacks were hungry to be part of the nation's home-owning mania. Loan officers, she said, pushed customers who could have qualified for prime loans into subprime mortgages. Another loan officer stated in an affidavit filed last week that employees had referred to blacks as "mud people" and to subprime lending as "ghetto loans."[9]

It would be misleading, however, to assume that disparities in lending levels between various racial and ethnic groups necessarily reflect discrimination. For example, while an analysis of Home Mortgage Disclosure Act data might show that subprime lending is disproportionately concentrated in low-income and minority neighborhoods,[10] reports indicate that similar conclusions could be reached based on such factors as age, sex, and marital status.[11] In addition, as more fully discussed in Part III hereof, disparities between different racial and ethnic groups *might* be explained by an examination of the specific creditworthiness of the individuals examined. For example, a study released in late 2008 revealed the following:

> 2004-2006 HMDA data showed that loans to minority borrowers had a substantially higher probability of exceeding the rate-spread reporting used by the regulators to define "high priced loans." These loans included both subprime and Alt-A loans … The data for all three years suggested that, on average, minority borrowers paid higher APRs for their mortgages than did non-minority borrowers.

* * *

> [But] [w]e were able to clearly demonstrate that the vast majority of APR differentials between minority and non-minority mortgage borrowers can be explained by observable characteristics appropriately associated with underwriting and pricing outcomes.[12]

As one of the panelists participating in the Commission's briefing on this topic noted, discrepancies between lending rates to various racial and ethnic groups might be the product of historical forces relating to wealth accumulation, as opposed to current discrimination.

---

[9] Michael Powell, *Bank Accused of Pushing Mortgage Deals on Blacks*, N.Y. TIMES, June 7, 2009, at A16. Allegations of discrimination in lending practices have led the NAACP to file a series of class action lawsuits against subprime lenders. *See* Jesse Washington, *NAACP to File Bias Suits Against Subprime Lenders*, WASH. POST, Mar. 14, 2009, at D03.

[10] *See*, *e.g.*, DEBBIE GRUENSTEIN BOCIAN, KEITH S. ERNST AND WEI LI, CTR. FOR RESPONSIBLE LENDING, UNFAIR LENDING: THE EFFECT OF RACE AND ETHNICITY ON THE PRICE OF SUBPRIME MORTGAGES 3 (May 2006) ("Our findings show that, for most types of subprime home loans, African-American and Latino borrowers are at greater risk of receiving higher-rate loans than white borrowers, even after controlling for legitimate risk factors.").

[11] *See* Joint U.S. Department of Housing and Urban Development and U.S. Department of Treasury Task Force on Predatory Lending, *Curbing Predatory Home Mortgage Lending*, June 2000, pp. 35-37 (hereinafter cited as Joint Task Force, *Curbing Predatory Home Mortgage Lending: A Joint Report*).

[12] Marsha J. Courchane, *Dawning of a New Age: Examination for Discrimination in Lending*, 27 No. 10 BANKING & FIN. SERVICES POL'Y REP. 1, 1, 7 (2008).

> [E]ven when we fully eradicate fraud and deception from the market, the fact will remain that, because of historical social injustice and inequality, African Americans and Hispanics have, on average, less access to credit than whites and other groups, on average, because these historically disadvantaged groups tend to have less household wealth, lower incomes, and lower credit scores on average than other groups.[13]

It is not possible for this report to reconcile the competing interpretations set forth above. It is possible, however, to examine the overall legal framework governing mortgage fraud and lending discrimination and the efforts undertaken by federal agencies to enforce these laws. Section I of this Part will examine the concept of predatory lending while Section II will examine mortgage fraud, and Section III will examine mortgage lending discrimination.

I. Predatory Lending

The term "predatory lending" is commonly used, but is not a legal term of art. That is to say, the term does not describe a uniform legal definition of specific acts. Depending how the term is used, it encompasses issues of mortgage fraud or lending discrimination, or aspects of both.

At the same time, a general consensus appears to exist that what is commonly called predatory lending involves lender practices that abuse the borrower through fraudulent, deceptive, or unfair loan terms or marketing practices. Such practices may or may not involve aspects of discrimination.

While there is no uniform agreement as to what constitutes predatory lending, the Federal Reserve uses the following simple but broad definition: "Targeting loans to elderly, low-income and other people to take advantage of their financial status or lack of financial knowledge."[14] The Office of the Comptroller of the Currency's (OCC) Guidelines Establishing Standards for Residential Mortgage Lending Practices list a number of practices that national banks should avoid.[15]

As stated, discrimination is not always at issue in predatory lending. For example, claims of predatory lending may be limited to seeking economic advantage through such practices as fraud, negligent misrepresentation, breach of fiduciary duty, or violations of consumer protection statutes,[16] including the Federal Trade Commission Act's (FTC Act) prohibition on unfair or deceptive acts or practices, found in Section 5 of the FTC Act.[17] Only when predatory terms and conditions have the purpose or

---

[13] Written statement of Brian P. Brooks to the U. S. Commission on Civil Rights, Mar. 20, 2009.

[14] Federal Reserve Bank of Dallas, *Building Wealth: A Beginner's Guide to Securing Your Financial Future*, 2002, p. 32, available at <http://www.dallasfed.org/ca/wealth/pdfs/wealth.pdf> (last accessed Aug. 4, 2009). *See also* ROBERT G. SCHWEMM, HOUSING DISCRIMINATION: LAW AND LITIGATION 18-8 n.33 (Thomson Reuters/West 2008) (citing Kathleen C. Engel, *Do Cities Have Standing? Redressing the Externalities of Predatory Lending,* 38 CONN. L. REV. 355, 356 n.6 (2006). (Professor Engel has found 'compelling evidence that the great bulk of subprime loans contain predatory terms.').

[15] 12 C.F.R. Part 30, App. C (2008).

[16] SCHWEMM, HOUSING DISCRIMINATION: LAW AND LITIGATION at pp. 18–8 to –9 n.34 (citing specific cases).

[17] 15 U.S.C. § 45(a) (2006).

effect of discriminating against minorities or other protected groups would they also present a violation of the Fair Housing Act, the Equal Credit Opportunity Act, or other civil rights laws.[18]

In a similar fashion, predatory lending is distinguishable from subprime lending.[19] Federal agencies, including OCC, the Board of Governors of the Federal Reserve, the Federal Deposit Insurance Corporation, the Office of Thrift Supervision, and the National Credit Union Administration, have issued joint guidance on subprime mortgage lending in July 2007.[20] The Guidance notes that, "subprime lending is not synonymous with predatory lending."[21] Subprime lending, in and of itself, simply reflects that some lenders are less creditworthy than others and, accordingly, pay higher interest rates or fees to obtain credit.

As noted by one of the panelists at the Commission's briefing on this topic:

> [T]here are significant benefits that must be weighed against the cost of defining "predatory lending" so broadly that it essentially eliminates the flow of credit to low- and moderate-income borrowers and borrowers with imperfect credit histories—borrowers who disproportionately tend to be members of minority groups.[22]

At the same time, there has been recognition that certain practices, often associated with certain types of subprime lending, are often linked with predatory lending practices. For example, the Guidance referenced above notes that certain adjustable rate mortgage (ARM) products present substantial risks to both consumers and lenders and are typically offered to subprime borrowers. These loans have one or more of the following characteristics:

> Low initial payments based on a fixed introductory rate that expires after a short period and then adjusts to a variable index rate plus a margin for the remaining term of the loan;
>
> * * *
>
> Very high or no limits on how much the payment amount or the interest rate may increase ("payment or rate caps") on reset dates;
>
> Limited or no documentation of borrowers' income;
>
> Product features likely to result in frequent refinancing to maintain an affordable monthly payment; and/or

---

[18] SCHWEMM, HOUSING DISCRIMINATION: LAW AND LITIGATION at pp. 18–8 to –10 n. 34–35 (citing specific cases).

[19] *See* Joint Task Force, *Curbing Predatory Home Mortgage Lending* at p. 47 ("Not all subprime lending is predatory, but predatory practices are most frequently found in connection with subprime lending.").

[20] Statement on Subprime Mortgage Lending, 72 Fed. Reg. 37569, 37573 (Dep't of the Treasury, Office of the Comptroller of the Currency; Fed. Reserve Sys.; Fed. Deposit Ins. Corp.; Dep't of the Treasury, Office of Thrift Supervision; and Nat'l Credit Union Admin. July 10, 2007).

[21] *Id.*

[22] Written statement of Brian P. Brooks to the U.S. Commission on Civil Rights, Mar. 20, 2009.

> Substantial prepayment penalties and/or repayment penalties that extend beyond the initial fixed interest rate period.[23]

Still, loans with such features, according to this Guidance, do not necessarily constitute predatory lending. Other factors are generally needed. For example, the Guidance notes that predatory lending typically involves at least one of the following elements:

> Making loans based predominantly on the foreclosure or liquidation value of a borrower's collateral rather than on the borrower's ability to repay the mortgage according to its terms;
>
> Inducing a borrower to repeatedly refinance a loan in order to charge high points and fees each time the loan is refinanced ("loan flipping"); or
>
> Engaging in fraud or deception to conceal the true nature of the mortgage loan obligation, or ancillary products, from an unsuspecting or unsophisticated borrower.[24]

A noted scholar on fair housing issues has defined predatory lending as "a syndrome of abusive loan terms or practices that involve one or more of the following five problems: (1) loans structured to result in seriously disproportionate net harm to borrowers, e.g., loans that contain unaffordable balloon payments, (2) harmful profit seeking, e.g., prepaid credit life insurance, (3) loans involving fraud or deceptive practices, (4) other forms of lack of transparency in loans that are not actionable as fraud, and (5) loans that require borrowers to waive meaningful legal redress."[25] For example, the National Community Reinvestment Coalition uses a broader definition:

> [A predatory loan is] an unsuitable loan designed to exploit vulnerable and unsophisticated borrowers. Predatory loans are a subset of subprime loans. A predatory loan has one or more of the following features: 1) charges more in interest and fees than is required to cover the added risk of lending to borrowers with credit imperfections, 2) contains abusive terms and conditions that trap borrowers and lead to increased indebtedness, 3) does not take into account the borrower's ability to repay the loan, and 4) violates fair lending laws by targeting women, minorities and communities of color.[26]

---

[23] Statement on Subprime Mortgage Lending, 72 Fed. Reg. at p. 37572.

[24] *Id.* at p. 37573.

[25] SCHWEMM, HOUSING DISCRIMINATION: LAW AND LITIGATION at p. 18-8 n.33 (citing Kathleen C. Engel & Patricia A. McCoy, *A Tale of Three Markets: The Law and Economics of Predatory Lending,* 80 TEX. L. REV. 1255, 1260–61 (2002)).

[26] NATIONAL COMMUNITY REINVESTMENT COALITION, THE BROKEN CREDIT SYSTEM: DISCRIMINATION AND UNEQUAL ACCESS TO AFFORDABLE LOANS BY RACE AND AGE (SUBPRIME LENDING IN TEN LARGE METROPOLITAN AREAS) 4 (2003), available at <http://www.omm.com/omm_distribution/newsletters/client_alert_financial_services/pdf/ncrcdiscrimstudy.pdf> (last accessed July 21, 2009). *See also* NATIONAL COMMISSION ON FAIR HOUSING AND EQUAL OPPORTUNITY, THE FUTURE OF FAIR HOUSING 31–36 (December 2008), available at <http://nationalfairhousing.org/Portals/33/reports/Future_of_Fair_Housing.PDF> (last accessed Aug. 4, 2009).

It is not the purpose of this report to reconcile these definitions. At this point it is sufficient to note that there is no accepted definition of what constitutes predatory lending. It should be noted, however, that the lack of a uniform definition precludes the collection of data relating to claims that might fall under the term of "predatory lending." As noted in a January 2004 report by the General Accounting Office:

> Currently no comprehensive and reliable data are available on the extent of predatory lending nationwide, for several reasons. First, the lack of a standard definition of what constitutes predatory lending makes it inherently difficult to measure. Second, any comprehensive data collection on predatory lending would require access to a representative sample of loans and information that can only be extracted manually from the physical loan files.[27]

Given these limitations, for purposes of reviewing enforcement efforts, this report examines the issue of mortgage fraud and lending discrimination in separate chapters.

II. Mortgage Fraud

A. Mortgage Fraud Generally

Mortgage fraud is "the intentional misstatement, misrepresentation, or omission by an applicant or other interested parties, relied on by a lender or underwriter to provide funding to purchase, or to insure a mortgage loan."[28]

Mortgage loan fraud encompasses many practices and can involve any or all parties to a transaction. Typical practices can include such schemes as misrepresentation of income or assets, the use of forged or fraudulent documents, misrepresentations as to intention to occupy property, fraudulent appraisals, identity fraud, and the use of straw buyers.[29]

---

[27] U.S. General Accounting Office, Report to the Chairman and Ranking Minority Member, Special Committee on Aging, U.S. Senate, *Consumer Protection: Federal and State Agencies Face Challenges in Combating Predatory Lending,* January 2004, p. 23, available at <http://www.gao.gov/new.items/d04280.pdf> (last accessed Aug. 4, 2009).

[28] Federal Bureau of Investigation, *2007 Mortgage Fraud Report,* April 2008 available at <http://www.fbi.gov/publications/fraud/mortgage_fraud07.htm> (last accessed Mar. 9, 2009) (hereinafter cited as *2007 Mortgage Fraud Report*).

[29] *See* U.S. Department of the Treasury, Financial Crimes Enforcement Network*, Mortgage Loan Fraud: An Update of Trends Based Upon an Analysis of Suspicious Activity Reports*, April 2008, available at <http://www.fincen.gov/news_room/rplfiles/MortgageLoanFraudSARAssessment.pdf> (last accessed Aug. 4, 2009). *See also* Press Release, DOJ, More Than 400 Defendants Charged for Roles in Mortgage Fraud Schemes as Part of Operation "Malicious Mortgage" (June 19, 2008) (Mortgage fraud schemes include "lending fraud, foreclosure rescue scams and mortgage-related bankruptcy schemes. Lending fraud frequently involves multiple loan transactions in which industry professionals construct mortgage transactions based on gross fraudulent misrepresentations about the borrower's financial status, such as overstating the borrower's income or assets, using false or fictitious employment records or inflating property values. Foreclosure rescue scams involve criminals who target legitimate homeowners in dire financial circumstances and fraudulently collect fees for foreclosure prevention services or obtain ownership interests in residential properties. Both of these fraudulent mortgage schemes may be furthered by filing bankruptcy petitions that automatically stay foreclosure.")

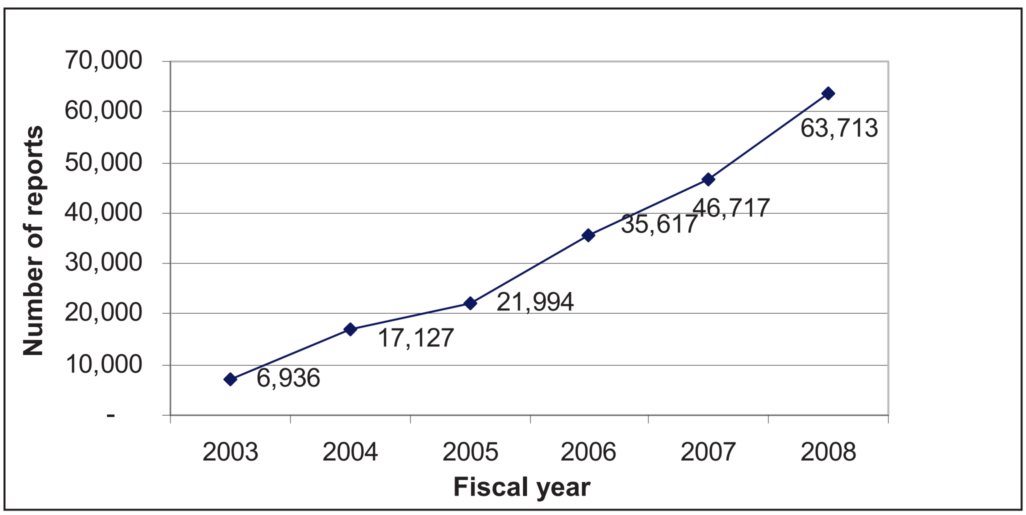
For example, a recent report by the Department of Treasury's Financial Crimes Enforcement Network indicated that borrowers were accused of wrongful acts in Suspicious Activity Reports (SARs) at almost the same rate as mortgage brokers, when the claim related to fraud for profit. Other participants included appraisers, investors, sellers, settlement agencies, and loan officers.[30]

By any standard, the rate of mortgage fraud reports has increased rapidly. According to the Federal Bureau of Investigation (FBI),

> Mortgage fraud continues to be an escalating problem in the United States. Although no central repository collects all mortgage fraud complaints, Suspicious Activity Reports (SARs) from financial institutions indicated an increase in mortgage fraud reporting. SARs increased 31-percent to 46,717 during Fiscal Year (FY) 2007. The total dollar loss attributed to mortgage fraud is unknown. However, 7 percent of SARs filed during FY 2007 indicated a specific dollar loss, which totaled more than $813 million.[31]

Since this statement was issued, figures for FY 2008 have been released, showing an even greater increase in mortgage fraud reporting to 63,713.

Figure 4.1
Financial Institutions' Mortgage Fraud-Related Suspicious Activity Reports, Fiscal Years 2003–2008



Sources: Federal Bureau of Investigation, *2007 Mortgage Fraud Report*, April 2008, *available at* <http://www.fbi.gov/publications/fraud/mortgage_fraud07.htm> (last accessed Aug. 4, 2009), p. 3 figure 1; Federal Bureau of Investigation, 2008 Mortgage Fraud Report, no date, *available at* <http://www.fbi.gov/publications/fraud/mortgage_fraud08.htm> (last accessed Aug. 4, 2009), p. 3 figure 1.

Caption: The number of mortgage fraud-related suspicious activity reports has steadily increased from 2003 to 2007, going from 6,936 reports in 2003 to 63,713 in 2008.

---

[30] U.S. Department of the Treasury, *Mortgage Loan Fraud*. *See also* Alyssa Katz, Our Lot: How Real Estate Came to Own Us 129-155 (2009) (detailing examples of fraud by borrowers).

[31] *2007 Mortgage Fraud Report.*

The rise and decline of subprime mortgage market has influenced mortgage fraud both directly and indirectly. As the bubble grew, and risk seemed to disappear, more and more individuals began to speculate or otherwise seek to benefit from rising values and inexpensive credit. The tone of the times is caught in the following description:

> Nearly everyone you met around Tampa had a Realtor's license or a broker's license or was a title agent. Alex Sink, the state's chief financial officer and a Democrat, said, 'When the yardman comes and says he's not going to mow your yard anymore because he's going to become a mortgage broker, that is a sure sign that something is wrong.' Flipping houses and condominiums turned into an amateur middle-class pursuit. People who drew modest salaries at their jobs not only owned a house but bought other houses as speculators, the way average Americans elsewhere dabble in day trading … There were secretaries with five to ten investment homes—a thirty-five thousand dollar salary and a million dollars in investments. There's no industry here, only houses.[32]

The extent of the frenzy at the height of the boom is reflected in the fact that, in 2005, almost 28 percent of all residential home purchases were made for investment purposes.[33]

As the market began to fall, incentives for fraud changed, but remained equally strong.

> During 2007 there were more than 2.2 million foreclosure filings reported on approximately 1.29 million properties nationally, up 75 percent from 2006. The declining housing market affects many in the mortgage industry who are paid by commission. During declining markets, mortgage fraud perpetrators may take advantage of industry personnel attempting to generate loans to maintain current standards of living.[34]

The FBI's 2008 report on mortgage fraud indicates that the top mortgage fraud states for 2008 were California, Florida, Georgia, Illinois, Michigan, Arizona, Texas, Maryland, Missouri, New Jersey, New York, Ohio, Colorado, Nevada, Minnesota, Rhode Island, the District of Columbia, Massachusetts, Pennsylvania, and Virginia.[35]

---

[32] George Packer, *The Ponzi State: Florida's Foreclosure Disaster*, NEW YORKER, Feb. 9 & 16, 2009, at p. 84. S*ee also* KATZ, OUR LOT: HOW REAL ESTATE CAME TO OWN US at pp. 156-84.

[33] *See 2009 National Association of Realtor®s Investment and Vacation Home Buyers Survey*, March 2005, p. 5; KATZ, OUR LOT: HOW REAL ESTATE CAME TO OWN US at pp. 116–17 ("In Sacramento, one out of every six loan applicants in 2005 admitted that they did not intend to live in the house they were financing — presumably, they were either intending to rent the property to tenants or to flip it quickly to a new owner.").

[34] *2007 Mortgage Fraud Report*. Alt-A loans may also be ripe for mortgage fraud because in many instances [they] do not require documentation of the borrower's income or assets, but rely instead on an applicant's statement, "making them ideal for fraud exploitation." *Id.* Losses involving Alt-A loans "were caused by income misrepresentations, employment frauds, straw buyers, investor-related frauds and occupancy frauds." *Id.*

[35] Federal Bureau of Investigation*, 2008 Mortgage Fraud Report,* no date*,* available at <http://www.fbi.gov/publications/fraud/mortgage_ fraud08.htm> (last accessed July 13, 2009) (hereinafter cited as *2008 Mortgage Fraud Report*)

B. Federal Enforcement Against Mortgage Fraud

No regulatory agency is solely responsible for pursuing perpetrators of mortgage fraud. Agencies involved in mortgage fraud investigations include the Department of Justice (DOJ), the Department of Housing and Urban Development's (HUD) Office of Inspector General, the Internal Revenue Service, the Postal Inspection Service, and state and local governments. Those agencies most relevant to other areas of this report, DOJ (including the FBI), HUD, and the Federal Trade Commission (FTC), are briefly addressed here:

1. The Department of Justice

DOJ investigates and prosecutes mortgage fraud, often in coordination with other federal and state agencies. Recent efforts, particularly by U.S. Attorneys' Offices, unearthed large numbers of defendants involved in wide-ranging mortgage schemes. In 2008, DOJ announced that its "Operation Malicious Mortgage" initiative resulted in 144 mortgage fraud cases involving 406 defendants from March 1 to June 18 of that year.[36]

Through this operation, DOJ brought charges in every region of the United States, exposing mortgage fraud schemes that had inflicted approximately $1 billion in losses, according to FBI estimates.[37] The FBI, the Postal Inspection Service, the Internal Revenue Service, the U.S. Immigration and Customs Enforcement, the U.S. Secret Service, the U.S. Trustee Program, HUD, the Department of Veterans Affairs, and the FDIC collaborated with DOJ in the Operation Malicious Mortgage effort.

In April 2009 a federal grand jury indicted four defendants (as well as an information against a fifth defendant) for their alleged participation in a "massive mortgage fraud scheme."[38]

A U.S. Attorney involved in the case reported that the indictment alleged that defendants convinced many victims to invest at least $50,000 by refinancing their existing homes or buying new homes at inflated prices, while claiming that Metro Dream Homes would repay the mortgages with revenue from profitable businesses … Instead, according to the indictment, the conspirators allegedly used some of the investors' money to repay earlier investors in the Ponzi scheme and spent the remainder on themselves.[39]

---

[36] Press Release, DOJ, More Than 400 Defendants Charged for Roles in Mortgage Fraud Schemes as Part of Operation "Malicious Mortgage" (June 19, 2008), available at <http://www.usdoj.gov/opa/pr/2008/June/08-odag-551.html> (last accessed Aug. 4, 2009).

[37] *Id.*

[38] Press Release, DOJ, Five Charged in $70 Million "Dream Home" Mortgage Fraud Scheme (April 27, 2009), available at <http://www.usdoj.gov/opa/pr/2009/April/09-crm-395.html> (last accessed Aug. 4, 2009).

[39] *Id.*

2. The Federal Bureau of Investigation

The FBI[40] "compiles data on mortgage fraud through Suspicious Activity Reports (SARs) filed by federally-insured financial institutions and HUD-OIG reports. The FBI also receives complaints from the mortgage industry at large."[41]

The FBI investigates mortgage fraud in two distinct areas: fraud for profit and fraud for housing:

> Fraud for profit is sometimes referred to as "Industry Insider Fraud," and the motive is to revolve equity, falsely inflate the value of the property, or issue loans based on fictitious properties. Based on existing investigations and mortgage fraud reporting, 80 percent of all reported fraud losses involve collaboration or collusion by industry insiders. Fraud for housing represents illegal actions perpetrated solely by the borrower. The simple motive behind this fraud is to acquire and maintain ownership of a house under false pretenses. This type of fraud is typified by a borrower who makes misrepresentations regarding his income or employment history to qualify for a loan.[42]

The Bureau reports it is focusing its efforts on mortgage fraud perpetrated by industry insiders. "The FBI is engaged with the mortgage industry primarily in identifying fraud trends and educating the public. Some of the current rising mortgage fraud trends include: equity skimming, property flipping, and mortgage related identity theft." [43]

As reflected in Figure 4.2, the number of pending FBI investigations has risen steadily in recent years, from 436 investigations in 2003 to 1,204 in 2007 and 1,644 in 2008.[44]

---

[40] An organization with its own headquarters, field offices in major cities throughout the United States, and over 30,000 employees, the FBI is part of the Department of Justice and reports to both the Attorney General and the Director of National Intelligence. FBI, *About Us — Quick Facts*, <http://www.fbi.gov/quickfacts.htm> (last accessed June 17, 2009).

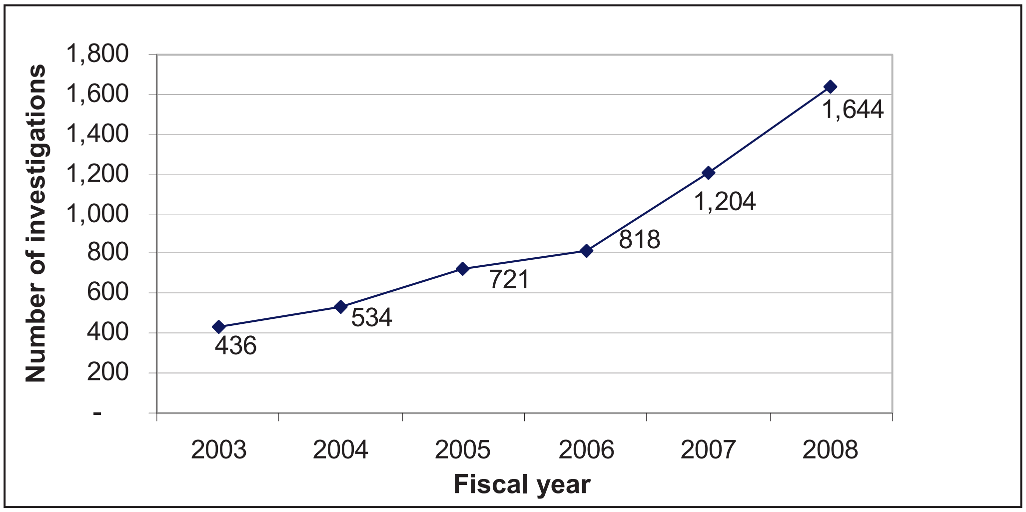
[41] FBI, *Financial Crimes Report to the Public*, Fiscal Year 2007, available at <http://www.fbi.gov/publications/financial/fcs_report2007/financial_crime_2007.htm#Mortgage> (last accessed April 30, 2009).

[42] *Id.*

[43] *Id.* ("Today's common equity skimming schemes involve the use of corporate shell companies, corporate identity theft, and the use or threat of bankruptcy/foreclosure to dupe homeowners and investors.") Property flipping is not a new phenomenon; but with it, "once again law enforcement is faced with an educated criminal element that is using identity theft, straw borrowers, shell companies, along with industry insiders, to conceal their methods and override lender controls." *Id.*

[44] *Id.*

Figure 4.2
FBI's Pending Investigations of Mortgage Fraud, Fiscal Years 2003–2008



Sources: Federal Bureau of Investigation, *2007 Mortgage Fraud Report*, April 2008, *available at* <http://www.fbi.gov/publications/fraud/mortgage_fraud07.htm> (last accessed Aug. 4, 2009), p. 7 figure 9; Federal Bureau of Investigation, *2008 Mortgage Fraud Report*, no date, *available at* <http://www.fbi.gov/publications/fraud/mortgage_fraud08.htm> (last accessed Aug. 4, 2009), p. 7 figure 10.

Caption: The number of FBI's pending investigations on mortgage fraud increased steadily in the period from 2003 to 2007, from 436 in 2003 to 1,644 in 2008.

3. The Department of Housing and Urban Development's Office of Inspector General

HUD-OIG investigates mortgage fraud related to FHA loans. According to former HUD Inspector General Kenneth Donohue, "FHA mortgages may be more prone to mortgage fraud because FHA insures mostly first-time homebuyers with limited credit histories and little money down."[45] HUD has investigated "thousands of cases of mortgage fraud" in the recent past and "repeatedly have found unlawful and deceptive practices and outright fraud in mortgage lending that often exploit first-time and uninformed FHA borrowers."[46]

According to HUD, mortgage fraud can go undetected, and some fraud results in no loss to the government. These facts "make it difficult to quantify the exact amount, or even an estimated amount, of mortgage fraud."[47]

Donohue provided examples of the types of scenarios that make mortgage fraud difficult to detect:

---

[45] HUD Inspector General Kenneth Donohue, Statement to the House Committee on Financial Services, Subcommittee on Housing and Community Opportunity (October 7, 2004), p. 2 (hereinafter cited as Donahue, Statement to the House Committee on Financial Services).

[46] *Id.* at p. 4. The FBI 2007 mortgage fraud study reported that HUD opened 239 single family mortgage fraud investigations in fiscal year 2006 and 151 in fiscal year 2007. The report indicates that HUD had a total of 466 loan investigations pending as of Sept. 30, 2007. The report attributes the 2006 to 2007 decrease in the number of opened investigations to a substantial decline in the FHA market share. *2007 Mortgage Fraud Report*.

[47] Donohue, Statement to the House Committee on Financial Services at p. 5.

> (1) the appraiser that was pressured by the lender for a higher appraisal value to match the sales price; (2) the homebuyer that submits false down payment gift letters; (3) the seller that works a side loan with the buyer in order to make the deal work; (4) the loan processor that overlooks a known debt that is not on the credit report. These things happen every day and all would be categorized as mortgage fraud, and these can go undetected unless the borrower defaults on the loan, or there is a pattern of defaults associated with a particular lender, realtor, or appraiser. Complicating every case of fraud is proving the perpetrator did it intentionally and showing significant loss to the Government."[48]

4. The Federal Trade Commission

The FTC is also involved in mortgage fraud, examining deceptive and unfair practices in its role as the primary agency enforcing consumer credit laws for nonbank financial companies, including nonbank mortgage companies, mortgage brokers, and finance companies.[49] The agency routinely coordinates enforcement activities with DOJ and HUD due to an overlap in fair lending jurisdiction.[50]

Among the actions targeted by the FTC are deceptive or unfair practices by mortgage lenders, brokers, and loan servicers in all stages of mortgage lending, from advertising and marketing to loan servicing, with particular emphasis on the subprime market. The majority of the agency's mortgage lending cases have challenged deception in advertising or marketing of subprime loans.[51] In fall 2008, the FTC reported that in the past decade it had initiated 23 actions against large and small companies and against principals in the mortgage lending industry throughout the country.[52] Over 320 million dollars have been returned to consumers as a result of large monetary judgments from several of these cases.[53]

Deceptive practices

The FTC reports that substantial enforcement efforts have also targeted mortgage brokers allegedly deceiving consumers about key loan terms, such as the existence of a prepayment penalty[54] or a large balloon payment due at the end of a loan.[55] The agency noted that in some of these cases it also has

---

[48] *Id.*

[49] For a summary, *see* Prepared Statement of the Federal Trade Commission on *Home Mortgage Disclosure Act Data and FTC Lending Enforcement* before the House Committee on Financial Services Subcommittee on Oversight and Investigations (July 25, 2007), pp. 7–9 (hereinafter cited as FTC Statement, *Lending Enforcement*); Prepared Statement of the Federal Trade Commission on *Improving Consumer Protections in Subprime Lending* before the Senate Committee on Commerce, Science, and Transportation Subcommittee on Interstate Commerce, Trade, and Tourism (Apr. 29, 2008), pp. 2, 4 (hereinafter cited as FTC Statement, *Consumer Protections*).

[50] FTC Statement, *Lending Enforcement* at p. 4.

[51] FTC Statement, *Consumer Protections* at p. 5.

[52] Press Release, Federal Trade Commission, Bear Stearns and EMC Mortgage to Pay $28 Million to Settle FTC Charges of Unlawful Mortgage Servicing and Debt Collection Practices (Sept. 9, 2008), available at <http://www.ftc.gov/opa/2008/09/emc.shtm> (last accessed April 24, 2009).

[53] *Id.*

[54] FTC Statement, *Consumer Protections* at *p*. 6 (citing *FTC v. Chase Fin. Funding*, No. 04-549 (C.D. Cal. 2004); *FTC v. Diamond*, No. 02-5078 (N.D. Ill. 2002)).

[55] FTC Statement, *Consumer Protections* at p. 6.

charged brokers with falsely promising consumers low fixed payments and rates on mortgage loans.[56] Representative deceptive practice actions include:

- In 2004 the FTC filed a lawsuit against a California mortgage broker, Chase Financial Funding (CFF), and its principals for sending unsolicited e-mail and direct mail promising "3.5% fixed payment loan."[57] The FTC alleged that what the CFF offered was in fact a "payment option" adjustable rate mortgage that accrued interest at a rate higher than advertised. Furthermore, according to the agency, the payments were not "fixed."[58]
- In 2006 the FTC filed a lawsuit against a mortgage broker for allegedly misrepresenting many key loan terms to Hispanic consumers.[59] The mortgage broker, the FTC alleged, conducted the business entirely in Spanish but provided at closing documents in English containing less favorable terms.[60] As a result, the mortgage broker has been permanently enjoined from misrepresenting loan terms.[61]

The FTC further reported that, as of April 2008, it was investigating more than a dozen mortgage companies as part of a mortgage advertising law enforcement sweep.[62] In September 2007, the agency sent warning letters to more than 200 mortgage brokers and lenders (as well as to the media outlets that carried their advertisements), advising them that some of their mortgage advertisements may be deceptive and in violation of Section 5 of the FTC Act[63] and/or TILA.[64] The FTC stated that it had reviewed advertisements of these mortgage brokers and will appropriately follow up with law enforcement.[65]

The FTC also challenges deceptive and unfair practices in the servicing of mortgage loans. Examples include:

- In 2008, Bear Stearns and its subsidiary, EMC Mortgage Corporation, agreed to pay $28 million to settle charges that they engaged in unlawful practices in servicing consumers' home mortgage

---

[56] *Id.*

[57] *Id.*, citing *FTC v. Chase Fin. Funding*, No. 04-549 (C.D. Cal. 2004).

[58] FTC Statement, *Consumer Protections* at pp. 6–7.

[59] *Id.* at *p*. 7 (citing *FTC v. Mortgages Para Hispanos.Com Corp.,* No. 06-00019 (E.D. Tex. Sept. 25, 2006)).

[60] *Id.*

[61] *Id.* (citing *FTC v. Mortgages Para Hispanos.Com Corp.*, No 06-00019 (E.D. Tex. Sept. 25, 2006)).

[62] *Id.*

[63] 15 U.S.C. §§ 41-58 (2006). Under this Act, the Commission is empowered, among other things, to (a) prevent unfair methods of competition and unfair or deceptive acts or practices; (b) bring civil actions and seek civil penalties for unfair or deceptive acts and practices; and (c) conduct investigations relating to the organization, business, practices, and management of entities engaged in commerce.

[64] FTC Statement, *Consumer Protections* at p. 7 (citing Press Release, Federal Trade Commission, FTC Warns Mortgage Advertisers and Media That Ads May Be Deceptive (Sept. 11, 2007), available at <http://www.ftc.gov/opa/2007/09/mortsurf.shtm> (last accessed Aug. 4, 2009).

[65] *Id.* at p. 8.

loans.[66] The companies allegedly misrepresented the amounts borrowers owed, charged unauthorized fees, such as late fees, property inspection fees, and loan modification fees, and engaged in unlawful and abusive collection practices.[67] Under the terms of the settlement, they were required to establish a data integrity program to ensure the accuracy and completeness of consumers' loan information.[68]

- In another case, the FTC and HUD settled with Fairbanks Capital Corporation (now known as Select Portfolio Servicing, Inc.) and its parent company in November 2003. The FTC alleged that Fairbanks failed to post consumers' payments upon receipt, charged unauthorized fees, used dishonest or abusive tactics to collect debts, and knowingly reported inaccurate consumer payment information to credit bureaus.[69]

The FTC has intensified law enforcement to protect consumers from mortgage foreclosure rescue scams because of the rapid increase in delinquency and foreclosure rates.[70] The agency reports that in 2007 there were 2.2 million foreclosures, a 75 percent increase from 2006.[71] While details may vary, it says that at the core of the foreclosure scam is a false promise that the firm will save a consumer's home.[72] Eight cases were brought within the space of approximately a year.[73] The defendants in these cases guaranteed they would obtain loan modification or stop foreclosure if the consumers paid up-front amounts of $500 to $2,000. The companies took the fees, but failed to obtain the promised relief. In two of the eight cases,[74] the FTC further alleged that the defendants falsely claimed affiliation with the non-profit, government-endorsed HOPE NOW Alliance, which offers free assistance in foreclosure prevention.[75]

---

[66] *Id.* at pp. 9–10.

[67] Prepared Statement of the Federal Trade Commission on *Leveraging FTC Resources to Protect Consumers of Financial Services and Promote Competition* before the House Committee on Appropriations Subcommittee on Financial Services and General Government (March 31, 2009), p. 4 (citing *FTC v. EMC Mortgage Corp*., No. 4:08-cv-338 (E.D. Texas Sept. 9, 2008)) (hereinafter cited as FTC Statement, *Leveraging FTC Resources*).

[68] *Id.*

[69] FTC Statement, *Consumer Protections* at p. 9 (citing *United States v. Fairbanks Capital Corp*., No. 03-12219 (D. Mass. 2003).

[70] *Id.* at p. 11.

[71] Prepared Statement of the Federal Trade Commission on *Foreclosure Rescue Fraud* before the Senate Special Committee on Aging, Washington, D.C. (February 13, 2008), p. 1.

[72] *Id.*.

[73] FTC Statement, *Leveraging FTC Resources* at p. 3 (citing *FTC v. Hope Now Modifications*, No. 1:09-cv-01204-JBS-JS (D.N.J. Mar. 17, 2009); *FTC v. New Hope Property LLC*, No. 1:09-cv-01203-JBS-JS (D.N.J. Mar. 17, 2009); *FTC v. National Foreclosure Relief, Inc.*, No. SACV09-117 (C.D. Cal. Feb. 2, 2009); *FTC v. United Home Savers, LLP*, No. 8:08-cv-01735-VMC-TBM (M.D. Fla. Sept. 3, 2008); *FTC v. Foreclosure Solutions, LLC*, No. 1:08-cv-01075 (N.D. Ohio Apr. 28, 2008); *FTC v. Mortgage Foreclosure Solutions, Inc.*, No. 8:08-cv-388-T-23EAJ (M.D. Fla. Feb. 26, 2008); *FTC v. National Hometeam Solutions, Inc.*, No. 4:08-cv-067 (E.D. Tex. Feb. 26, 2008); *FTC v. Safe Harbour Foundation*, No. 08 C 1185 (N.D. Ill. Feb. 25, 2008)).

[74] *Id.* at p. 3 (citing FTC *v. Hope Now Modifications*, No. 1:09-cv-01204-JBS-JS (D.N.J. March 17, 2009); *FTC v. New Hope Property LLC,* No. 1:09-cv-01203-JBS-JS (D.N.J. March 17, 2009)).

[75]*Id.*

III. Mortgage Lending Discrimination

Mortgage lending discrimination encompasses loans with a variety of purposes including purchasing or refinancing homes and financing home improvements.[76] Refinancing includes efforts to reduce interest rates or alter the term of the loan or extracting cash from home equity. Borrowers may have, in addition to a first lien, a smaller junior lien, that would allow a borrower to access home equity or to avoid having to secure mortgage insurance on the first lien.[77]

The mortgages that financial institutions make to individual borrowers are often bought by financial institutions in the secondary mortgage market. The home mortgages may be securitized[78] by the federal Government National Mortgage Association (Ginnie Mae), Fannie Mae, Freddie Mac, or private securitizers.

Mortgage lending discrimination may occur in a variety of different ways, but often arises when mortgage lenders treat similarly situated borrowers differently because of membership in a protected class.[79] For example, lenders may refuse to offer credit at all to certain types of groups or individuals.[80] Early financial discrimination cases generally involved complaints of minorities or residents of minority neighborhoods that lenders rejected their applications for mortgage credit.[81]

"Redlining" is a specific type of mortgage lending discrimination in which lenders deny home loans based on the characteristics of the would-be borrower's neighborhood. When based on the race, color, national origin, sex, religion, disability, or familial status of persons, such denials may constitute discrimination in violation of the Fair Housing Act. In addition, when based on race, color, national origin, sex, religion, marital status, or age, such denials may constitute discrimination in violation of the

---

[76] SCHWEMM, HOUSING DISCRIMINATION: LAW AND LITIGATION at p. 18-11 (citing 42 U.S.C. § 3605 (1982 & Supp. 1987).

[77] The present examination analyzes both loans for home purchases and refinancing, sometimes together and sometimes separately. Some analyses examine first liens only, and others both first and junior liens. In the secondary mortgage market, the Commission directed its attention primarily to Fannie Mae and Freddie Mac, or the government-sponsored enterprises collectively, although some analyses present data for the market as a whole or contrast the GSEs with other types of financial institutions.

[78] The process by which mortgage loans are sold to investors is securitization. Mortgage loans are purchased from loan originators (such as banks or mortgage companies) by government or private entities that group or "pool" individual mortgage loans with certain characteristics. The mortgage-backed securities (usually with a Fannie Mae, Freddie Mac, or Ginnie Mae guarantee) were sold to investors as bonds.

[79] ANDREW HAUGHWOUT, CHRISTOPHER MAYER, AND JOSEPH TRACY, FEDERAL RESERVE BANK OF NEW YORK, SUBPRIME MORTGAGE PRICING: THE IMPACT OF RACE, ETHNICITY, AND GENDER ON THE COST OF BORROWING, staff report no. 368 April 2009, p. 3, <http://www.newyorkfed.org/research/staff_reports/sr368.pdf> (last accessed July 17, 2009).

[80] *Id.*

[81] SCHWEMM, HOUSING DISCRIMINATION: LAW AND LITIGATION at pp. 18–7 to –8 (attributing such cases to "the early years of the 1968 Fair Housing Act."). *See also* Christine Robitscher Ladd, *"Federal Fair Housing Enforcement: The Clinton Record at the End of the First Term,"* in CITIZENS' COMMISSION ON CIVIL RIGHTS, THE CONTINUING STRUGGLE: CIVIL RIGHTS AND THE CLINTON ADMINISTRATION 229 (1997), <http://www.ccr.org/doc/struggle.pdf> (last accessed July 17, 2009) (where the author distinguishes a 1995 Department of Justice case (*U.S. v. Northern Trust Company*), which, along with earlier ones that also involved allegations of discrimination in underwriting, led to loan rejections, from 1996 cases that concerned discrimination in the pricing of loans.).

Equal Credit Opportunity Act.[82] Nevertheless, financial institutions may consider factors such as individual creditworthiness of borrowers, when evaluated in a non-discriminatory fashion, and which are justified by business necessity.[83] Redlining may also include "reverse redlining," which is the practice of targeting certain borrowers or areas with less advantageous products or services based on prohibited characteristics.

Since the passage of the Fair Housing Act in 1968, Congress has enacted additional statutes to combat housing and mortgage lending discrimination, the most relevant to this report being the Equal Credit Opportunity Act.[84] Additional consumer protection statutes related to lending include the Truth in Lending Act, the Home Ownership and Equity Protection Act, the Real Estate Settlement Procedures Act, the Home Mortgage Disclosure Act, and the Federal Housing Enterprises Financial Safety and Soundness Act of 1992. Enforcement of these laws involves no less than nine federal agencies – and in some instances many more. The diffuse nature of jurisdiction arises from the fact that oversight has been assigned based on the type of entity covered. Thus, generally:

- The Board of Governors of the Federal Reserve System (the Federal Reserve) oversees bank holding companies, nonbank subsidiaries of bank holding companies, State-chartered banks that are members of the Federal Reserve System, and the U.S. operations of foreign banking organizations. It also regulates the foreign activities and investments of the Federal Reserve member banks, and Edge Act corporations.
- The Office of the Comptroller of the Currency (OCC) supervises national banks and federal branches and agencies of foreign banks.
- The Federal Deposit Insurance Corporation (the FDIC) oversees State-chartered banks and savings banks that are not members of the Federal Reserve System and foreign banks having insured branches.
- The Office of Thrift Supervision (OTS) oversees federal savings associations and also supervises State-chartered thrifts and thrift holding companies.
- The National Credit Union Association (NCUA) oversees federal credit unions, including state-chartered credit unions.
- The Federal Trade Commission (the FTC) oversees mortgage brokers and non-bank mortgage lenders.
- The Department of Housing and Urban Development (HUD) administers and enforces the Fair Housing Act, and the Real Estate Settlement Procedures Act provisions applicable to all

---

[82] SCHWEMM, HOUSING DISCRIMINATION: LAW AND LITIGATION at pp. 18-22 to -23.

[83] *Id.* at p. 18-24.

[84] Precursors to the Fair Housing Act that prohibited certain forms of discrimination in housing and/or mortgage lending included Title VI of the Civil Rights Act of 1964, 42 U.S.C. § 2000d et seq., which bars discrimination on the basis of race, color, or national origin in programs and activities receiving federal financial assistance. Executive Order 11063 (1962), which bars discrimination in the sale, leasing, rental, or other disposition of properties and facilities owned or operated by the federal government or provided with federal funds, 42 U.S.C. § 1982, which provides all citizens of the United States with the same rights "enjoyed by white citizens … to inherit, purchase, lease, sell, hold, and convey real and personal property," and the Fourteenth Amendment to the Constitution which guarantees "the equal protection of the laws."

federally related mortgage loans and administers the fair lending provisions of the Federal Housing Enterprises Financial Safety Act.

- The Department of Justice (DOJ) enforces applicable fair housing and fair lending laws against all entities which may have engaged in a pattern or practice of discrimination, regardless of the type of entity.[85]

A. *Statutory Efforts to Protect Mortgage Applicants and Borrowers*

1. Fair Housing Act

Title VIII of the Civil Rights Act of 1968, also known as the Fair Housing Act (FHA), remains at the center of the federal government's efforts to eliminate housing discrimination.[86] FHA is based on "the policy of the United States to provide, within constitutional limitations, for fair housing throughout the United States."[87] It was subsequently amended in 1974 and again in 1988 to expand coverage of the Act and to expand enforcement options by both private plaintiffs and the federal government.

FHA prohibits, among other things, discrimination in the sale or rental of housing, including the provision of brokerage services, on the basis of race, color, religion, national origin, sex, familial status, or disability.[88] FHA also prohibits discrimination in the residential lending process. Finally, it also makes it unlawful for a person to coerce, intimidate, threaten, or interfere with another person's rights under FHA.[89]

FHA is administered by HUD. In addition to its own enforcement efforts, HUD also works with government (federal and state) and non-governmental entities to formulate and carry out programs to prevent or eliminate discriminatory housing practices. Furthermore, HUD cooperates with and renders technical and other assistance to the Community Relations Service (a component of DOJ) to prevent or eliminate discriminatory housing practices.[90] HUD is also charged with initiating educational and conciliatory activities to further the purpose of FHA.[91]

In addition to adding familial status and disability as protected classes under FHA, the 1988 Fair Housing Amendments Act created an administrative enforcement system that is subject to judicial review. Prior to 1988, HUD could only investigate and conciliate complaints of housing

---

[85] The diffuse nature of enforcement was recently examined in a study prepared by the U.S. Government Accountability Office. *See* U.S. Gov't Accountability Office, GAO-09-704, Fair Lending: Data Limitations and the Fragmented U.S. Financial Regulatory Structure Challenge Federal Oversight and Enforcement Efforts (July 2009).

[86] Fair Housing Act of 1968, Pub. L. No. 90-284, 82 Stat. 81 (codified at 42 U.S.C. §§ 3601–3619 (2004)).

[87] 42 U.S.C. § 3601 (2006).

[88] *Id.* § 3604. Race, color, religion, and national origin were the original protected bases covered by Title VIII of the Civil Rights Act of 1968. Pub. L. 90-284, Title VIII, § 804, Apr. 11, 1968, 82 Stat. 83. Sex was added by the 1974 amendments. Pub. L. 93-383, Title VIII § 808(b)(1), Aug. 22, 1974, 88 Stat. 729. Familial status and disability, or handicap, were added by the 1988 amendments. Pub. L. 100-430, §§ 6(a)–(b)(2), (e), 15, Sept. 13, 1988, 102 Stat. 1620, 1622, 1623, 1636.

[89] 42 U.S.C. § 3617 (2006).

[90] Civil Rights Act of 1964, 42 U.S.C. § 2000g-1 (2006).

[91] 42 U.S.C. § 3609 (2006).

discrimination.[92] With the adoption of the 1988 amendments, if HUD's investigation of a HUD-filed complaint determines that there was reasonable cause to believe that the respondents violated FHA, and the complaint cannot be conciliated, HUD will issue a Charge of Discrimination which is adjudicated before an Administrative Law Judge unless one of the parties elects to litigate the Charge in federal District Court.[93]

In addition to the efforts of HUD, DOJ, through its Civil Rights Division's Housing and Civil Enforcement Section, also enforces FHA. DOJ has the primary responsibility for initiating litigation relating to pattern or practice violations of FHA, but the Attorney General is also authorized to pursue pattern or practice or land use and zoning discrimination cases referred by HUD.[94] Moreover, individuals who claim violations of FHA or the respondents in those matters can elect to have the matter heard in federal court, in which case DOJ brings the action on the complainant's behalf, otherwise, the matter will go before an Administrative Law Judge at HUD. The individual claiming to be aggrieved also can file a private cause of action in federal court.[95]

The federal banking agencies (the FDIC, OCC, OTS, and Federal Reserve Board) regularly examine the insured depository institutions (banks and thrifts) that they supervise for fair lending compliance including compliance with FHA. The federal banking agencies may take administrative enforcement actions (cease and desist orders, civil money penalties, etc.) to address any violations of law or regulation, including FHA. If a federal banking agency has a reason to believe that a "pattern or practice" of discrimination of FHA has occurred, the agency must make a referral to DOJ for enforcement.

The goals of FHA are furthered through the Fair Housing Initiatives Program (FHIP) and the Fair Housing Assistance Program (FHAP) supervised by HUD.[96] Through FHIP, HUD provides funding to fair housing organizations, and non-profits and other private entities which assist individuals who believe they have been discriminated against in housing. In addition to helping organizations carry out enforcement and education initiatives, such funding also enables recipients to send "testers" to property holders or managers suspected of housing discrimination.[97] Through FHAP, HUD provides funding to state and local agencies that enforce fair housing laws substantially equivalent to FHA. This funding is typically provided for the purposes of capacity building, using "testers," complaint processing,

---

[92] U.S. Commission on Civil Rights, *The Fair Housing Amendments Act of 1988: The Enforcement Report*, September 1994, p. 5.

[93] 42 U.S.C. §§ 3610, 3612 (2006).

[94] *Id.* § 3614.4.

[95] *Id.* §§ 3610–3613.

[96] *Id.* § 3616a(a).

[97] Testers have been defined, for example, as "minorities and whites with the same financial qualifications who evaluate whether housing providers treat equally-qualified people differently." U.S. Department of Housing and Urban Development, *Fair House Assistance Program*, <http://www.hud.gov/offices/fheo/partners/FHIP/fhip.cfm> (last accessed Apr. 1, 2009). *See also* SCHWEMM, HOUSING DISCRIMINATION: LAW AND LITIGATION at pp. 16-4 to -5.

administrative costs, special enforcement efforts, training, and other projects related to enforcing fair housing law.[98]

2. Equal Credit Opportunity Act

The Equal Credit Opportunity Act (ECOA) was enacted in 1974 and later amended in 1976 as Title VII of the Consumer Credit Protection Act.[99] Additional detail is provided by Regulation B, promulgated by the Federal Reserve, which identifies ECOA's purpose as:

> [T]o promote the availability of credit to all creditworthy applicants without regard to race, color, religion, national origin, sex, marital status, or age; or to the fact that all or part of the applicant's income derives from a public assistance program; or to the fact that the applicant has in good faith exercised any right under the Consumer Credit Protection Act.[100]

ECOA and Regulation B prohibit discrimination against an applicant for credit on the basis of race, color, religion, national origin, sex or marital status, age (provided the applicant has the capacity to contract), the applicant's acceptance of public assistance, or the applicant's good faith exercise of rights under ECOA.[101]

In total, 11 agencies plus DOJ have specific administrative enforcement powers under ECOA with differing jurisdiction based on the type of entity regulated, as described later in this chapter[102]: (1) the Federal Reserve; (2) OCC; (3) the FDIC; (4) OTS; (5) NCUA; (6) the U.S. Department of Transportation; (7) the U.S. Department of Agriculture; (8) the Farm Credit Administration; (9) the U.S. Securities and Exchange Commission; (10) the Small Business Administration; and (11) the FTC.[103] These agencies may initiate administrative proceedings against a covered entity who fails to comply with ECOA.[104]

In addition to the above, OCC, the Federal Reserve, the FDIC, OTS, and NCUA must refer any matter to the Attorney General if there is a pattern or practice of discouraging or denying applications for credit that violates the Act.[105] These agencies also have the discretion to refer the matter to the Attorney

---

[98] U.S. Department of Housing and Urban Development, *Fair House Assistance Program*, <http://www.hud.gov/offices/fheo/partners/FHAP/index.cfm> (last accessed Apr. 1, 2009).

[99] Equal Credit Opportunity Act, Pub. L. No. 93-495, 88 Stat. 1521 (1974), Pub. L. No. 94-234, 90 Stat. 253 (1976) (codified at 15 U.S.C. §§ 1691-1691f (2006)).

[100] Equal Credit Opportunity Act (Regulation B), 12 C.F.R. § 202.1(b) (2008).

[101] 15 U.S.C. § 1691(a) (2006).

[102] The nature of such enforcement powers was recently examined in a report by the U.S. Government Accountability Office. *See* U.S. Gov't Accountability Office, GAO-09-704, Fair Lending: Data Limitations and the Fragmented U.S. Financial Regulatory Structure Challenge Federal Oversight and Enforcement Efforts (July 2009).

[103] *Id.* § 1691c.

[104] OTS may also bring an enforcement action for noncompliance with its Nondiscrimination Rule (12 C.F.R., part 528), which supplements ECOA and the FHA.

[105] 15 U.S.C. § 1691e(g) (2006).

General if one or more creditors are suspected of violating ECOA.[106] Under this second scenario, if the agency chooses not to refer the matter to the Attorney General, but the agency believes the matter is also a violation of FHA, it is required to notify the Secretary of HUD, and to inform the applicant of the possible availability of remedies under FHA.[107] Further, Executive Order 12892 provides that, upon receipt of a complaint alleging facts that may constitute a violation of the FHA or upon receipt of information from a consumer compliance examination or other information suggesting a violation of the FHA, each executive agency shall forward such facts or information to the Secretary of HUD.[108] Where such facts or information indicate a possible pattern or practice of discrimination in violation of the Act, they also shall be forwarded to the Attorney General.[109]

The Attorney General may also independently institute appropriate civil actions when he or she believes that there is a pattern or practice that violates ECOA.[110]

Finally, ECOA provides a private right of action for applicants for credit who believe they have been discriminated against.[111]

3. Truth in Lending Act

The Truth in Lending Act (TILA) was enacted in 1968 to protect consumers in the use of credit.[112] For the mortgage industry, the Act's stated goal is "to assure a meaningful disclosure of credit terms so that the consumer will be able to compare more readily the various credit terms available to him [or her] and avoid the uninformed use of credit, and to protect the consumer against inaccurate and unfair credit billing and credit card practices."[113]

TILA applies to various types of credit, but for the purposes of this study, its most relevant application is to "open end" and "closed end" credit secured by a consumer's dwelling or residential property.[114] In addition to providing meaningful disclosure of terms such as the finance charge, the annual percentage

---

[106] *Id.*

[107] *Id.* § 1691e(k).

[108] Executive Order No. 12,892, 59 Fed. Reg. 2939 (Jan. 20, 1994).

[109] *Id.*

[110] 15 U.S.C. § 1691e(h) (2006).

[111] *Id.* § 1691e.

[112] Truth in Lending Act, Pub.L. 90-321, 82 Stat. 146 (1968) (codified at 15 U.S.C. §§ 1601–1667 (2006)).

[113] 15 U.S.C. § 1601(a) (2006). TILA was also enacted to protect consumers when leasing personal property also through meaningful disclosure of terms "so as to enable the lessee to compare more readily the various lease terms available to him [or her], limit balloon payments in consumer leasing, enable comparison of lease terms with credit terms where appropriate, and to assure meaningful and accurate disclosures of lease terms in advertisements." 15 U.S.C. § 1601(b).

[114] Open end credit is "consumer credit extended by a creditor under a plan in which: [1] the creditor reasonably contemplates repeated transactions; [2] the creditor may impose a finance charge from time to time on an outstanding unpaid balance; and [3] the amount of credit that may be extended to the consumer during the term of the plan (up to any limit set by the creditor) is generally made available to the extent that any outstanding balance is repaid." 12 C.F.R. § 226.2(a)(20) (2008). Regulation Z defines closed end credit as any type of credit other than open end credit. *Id.* § 226.2(a)(10).

rate (APR), the amount financed, and the total of all payments,[115] TILA provides, in certain circumstances, consumers the right to rescind a home equity or refinance mortgage within three days of the closing, the delivery of the rescission forms, or the statement containing the material disclosures required by TILA.[116]

Under the Act, the Federal Reserve is responsible for creating regulations to implement the law. These regulations have come to be known as Regulation Z codified in Part 226 of Title 12 of the Code of Federal Regulations. In addition to promoting the informed use of consumer credit through disclosures about terms and cost, Regulation Z also "gives consumers the right to cancel certain credit transactions that involve a lien on a consumer's principal dwelling, regulates certain credit card practices, and provides a means for fair and timely resolution of credit billing disputes."[117] Regulation Z was substantially revised in 2008, as a response to the current mortgage crisis, but most of those changes will not go into effect until October 1, 2009.[118]

TILA is enforced by a variety of federal agencies, depending on the entities each agency regulates. These agencies are: (1) OCC; (2) the Federal Reserve; (3) the FDIC; (4) OTS; (5) NCUA; (6) the U.S. Department of Transportation (DOT); (7) the U.S. Department of Agriculture (USDA); (8) the Farm Credit Administration; and (9) the FTC, which has overall enforcement power.[119]

As to enforcement, these agencies can pursue administrative proceedings against suspected violators of TILA.[120] State attorneys general may also pursue violators of TILA, but must inform the relevant agency and the agency can choose to intervene in the action or file a petition for appeal.[121] A private right of action exists for individuals who believe their TILA rights have been violated.[122] In addition, criminal liability exists for willfully and knowingly violating the statute.[123]

4. Home Ownership and Equity Protection Act

In 1994, TILA was amended by the Home Ownership and Equity Protection Act (HOEPA) in order to address deceptive and unfair practices in certain types of mortgage loans with high rates and/or high fees.[124] HOEPA establishes requirements for closed-end refinance mortgage loans and closed-end home equity loans (1) with interest rates greater than 8 percentage points for first-lien loans or 10 percentage

---

[115] 15 U.S.C. §§ 1631–1638. Note that the terms required to be disclosed depends on whether the loan is classified as open end or closed end credit.

[116] *Id.* § 1635(a).

[117] 12 C.F.R. § 226.1(b) (2008).

[118] 73 Fed. Reg. 44,522–44,614 (July 30, 2008) (to be codified at 12 C.F.R. pt. 226).

[119] 15 U.S.C. § 1607 (a),(c) (2006).

[120] *Id.* § 1607.

[121] *Id.* § 1640(e).

[122] *Id.* § 1640(a).

[123] *Id.* §§ 1611–1612.

[124] Home Ownership and Equity Protection Act, 15 U.S.C. § 1639 (1994).

points for subordinate-lien loans above comparable Treasury securities; or (2) where the total points and fees paid by the consumer at or before closing is greater than 8 percent of the loan amount or a set dollar amount (for example, in 2009 the amount is $583).[125] HOEPA excludes from coverage purchase money mortgages, reverse mortgages, and open-end credit plans.[126] Pursuant to 12 U.S.C. § 1639(l), the Federal Reserve promulgated section 32 of Regulation Z to implement HOEPA.[127]

HOEPA's goals are essentially two-fold: to provide additional disclosures to consumers for loans with high rates and/or high fees, and to prohibit certain terms in such loans. HOEPA also provides private and administrative remedies for violations of the Act.

HOEPA also requires lenders to provide additional disclosures to borrowers regarding their right to not complete the loan transaction even after beginning the process, the consequence of foreclosure and penalties if payment is not made, and terms of the loan including the APR and loan amount.[128] HOEPA which is an amendment to TILA, provides that any mortgage that contains a provision prohibited under HOEPA is deemed to be a failure to deliver the material disclosures required under TILA for purposes of TILA's right of rescission provisions (found in 15 U.S.C § 1635).[129] Summarized, HOEPA prohibits the following:

In general, HOEPA prohibits the following:

- Most prepayment penalties.[130]
- Loans with default interest rates that are higher than the interest rate that applies before the default.[131]
- Balloon payments for loans with less than five-year terms.[132]
- Loans with negative amortization.[133]

---

[125] 15 U.S.C. § 1602(aa) and 12 C.F.R. §226.32(a) (2008). The set fee cap is adjusted annually by the Federal Reserve using the Consumer Price Index. 15 U.S.C. § 1602(aa)(3) (2006).

[126] 15 U.S.C. § 1602(aa)(1) (2006).

[127] 12 C.F.R. § 226.32 (2008).

[128] 15 U.S.C. § 1639(a) (2006). Specifically, the following disclosures must be made: (1) "You are not required to complete this agreement merely because you have received these disclosures or have signed a loan application;" and (2) "If you obtain this loan, the lender will have a mortgage on your home. You could lose your home, and any money you have put into it, if you do not meet your obligations under the loan." *Id.* § 1639(a)(1). In addition, HOEPA requires disclosures related to APRs, amount of regular monthly payment, statement regarding interest rate and that the monthly payment may increase for variable interest credit transactions, and the amount of maximum monthly payment for variable interest credit transactions. *Id.* § 1639(a)(2).

[129] *Id.* § 1639(j).

[130] *Id.* § 1639(c)(1)(A).

[131] *Id.* § 1639(d).

[132] *Id.* § 1639(e).

[133] *Id.* § 1639(f).

- Loans that require prepayment at closing of more than two periodic payments.[134]
- Loans based on the value of the consumer's property without regard to the consumer's ability to repay the loan.[135]
- Creditor direct payments to home improvement contractors.[136]

As aforementioned, a violation of HOEPA constitutes a violation of TILA.[137] Thus, all recourse available under TILA applies to HOEPA loans as well. In addition, civil penalties may be assessed.[138]

5. Real Estate Settlement Procedures Act

The Real Estate Settlement Procedures Act (RESPA) was passed in 1974 after Congress found that significant reform in the real estate settlement process was needed to ensure that consumers were provided greater and more timely information concerning the nature and the costs of the settlement process.[139] In particular, Congress was concerned with unnecessarily high settlement charges and abusive practices that had developed throughout the country.[140]

RESPA requires that consumers receive disclosures at three distinct periods in the residential property transaction: at the time of application, at closing, and after the closing.[141] It also prohibits practices that tend to increase the cost of settlement services, including kickbacks and unearned fees.[142] and limits the amount home buyers are required to place in escrow accounts established to ensure the payment of real estate taxes and insurance.[143] Finally, it places the choice of title insurance provider with the buyer.[144]

RESPA applies to transactions involving a "federally related mortgage loan" and to "persons," which include entities and individuals.[145] The Act's provisions apply especially to those persons who and entities that provide "settlement services,"[146] including: (1) mortgage bankers and mortgage brokers; (2) real estate brokers and agents; (3) title companies and title agents; (4) settlement agents; (5) home

---

[134] *Id.* § 1639(g).

[135] *Id.* § 1639(h).

[136] *Id.* § 1639(i). Proceeds for home improvement loans must be disbursed either directly to the consumer, jointly to the consumer and the home improvement contractor, or, in some instances, to the escrow agent.

[137] *Id.* § 1639(j).

[138] Section 8 of the FDI Act, 12 U.S.C. § 1818(h).

[139] Real Estate Settlement Procedures Act of 1974, Pub. L. No. 93-533, 88 Stat. 1724 (codified at 12 U.S.C. §§ 2601 – 2617) (1974).

[140] 12 U.S.C. § 2601(a) (2006).

[141] *Id.* §§ 2602 – 2609.

[142] *Id.* § 2607.

[143] *Id.* § 2609.

[144] *Id.* § 2608(a).

[145] *Id.* § 2602.

[146] *Id.* § 2602.

warranty companies; (6) hazard insurance agents; (7) appraisers; (8) flood and tax service providers; and (9) others.[147]

RESPA also requires mortgage servicers to respond within 20 days to a "qualified written request" submitted by a borrower related to the servicing of a mortgage loan. The mortgage servicer has 60 days after the receipt of the borrower inquiry to conduct an investigation and make appropriate corrections to the account or to provide the borrower with a written explanation or clarification of the reason the servicer believes the account is correct. During that investigation period, the servicer may not report an overdue payment to a consumer reporting agency.[148]

HUD is responsible for promulgating rules on enforcing RESPA. In addition, the federal banking agencies examine for and enforce compliance with RESPA's requirements with respect to the institutions they supervise.[149] Section 2617(a) authorizes the Secretary of HUD to prescribe rules and regulations, make interpretations, and grant exemptions for classes of transactions as necessary to achieve the purposes of the Act.[150] The Act also mandates certain disclosures, including the good faith estimate,[151] a standard form for the statement of settlement costs (known as the HUD-1 or HUD-1A)[152] and escrow disclosures.[153]

RESPA also provides remedies for some violations of its provisions. Depending on the type of violation, borrowers, HUD, and certain state officials may bring actions under RESPA:

> (1) A borrower may bring a private lawsuit, or a group of borrowers may bring a class action suit, against a servicer who violates the servicing provisions of RESPA;
>
> (2) HUD may investigate and penalize loan servicers that violate the escrow account provisions of RESPA;[154]
>
> (3) Violators of RESPA's provisions against kickbacks and fee-splitting can be pursued by the Secretary of HUD, the Attorney General of any state, the insurance commissioner of any state, or an individual borrower;[155] and

---

[147] 24 C.F.R. § 3500.2 (2008).

[148] *Id.* § 3500.21.

[149] *See* 24 C.F.R. § 35300.19(a) ("It is the policy of the [HUD] Secretary regarding RESPA enforcement matters to cooperate with Federal, State, or local agencies having supervisory powers over lenders or other persons with responsibilities under RESPA. Federal agencies with supervisory powers over lenders may use their powers to require compliance with RESPA.").

[150] 12 U.S.C. § 2617(a) (2006).

[151] *Id.* § 2604.

[152] *Id.* § 2603.

[153] *Id.* § 2609.

[154] *Id.*

[155] *Id.* § 2607.

(4) Violations of the title insurance provisions may be pursued by the Secretary of HUD, the Attorney General of any state, or the insurance commissioner of any state, or an individual borrower.[156]

6. Home Mortgage Disclosure Act

The Home Mortgage Disclosure Act (HMDA) was passed in 1975 to "provide the citizens and public officials of the United States with sufficient information to enable them to determine whether depository institutions are filling their obligations to serve the housing needs of the communities and neighborhoods in which they are located and to assist public officials in their determination of the distribution of public sector investments in a manner designed to improve the private investment environment."[157] In addition, HMDA provides loan data to assist in identifying possible discriminatory lending patterns.[158] The Act provides the Federal Reserve the general power to prescribe regulations as necessary to carry out the purpose of HMDA.[159] Pursuant to this authority, the Federal Reserve has promulgated Regulation C in order to effectuate the purpose of HMDA.[160]

Generally, HMDA applies to "depository institutions"[161] and "other lending institutions."[162] Section 2802(A) of HMDA defines the term "depository institution" as any bank, savings association, and any credit union, which makes federally related mortgage loans. "Other lending institutions" are defined as non-depository institutions such as savings and loans, mortgage banking subsidiaries of bank holding companies, savings and loan holding companies, and independent mortgage lenders.

HMDA requires covered entities to compile lending data about home purchase loans annually and make this information public. The data collected include: race, ethnicity, minority status, income, gender, type of loan, purchaser of loan, disposition of loan applications, reasons for denial of applications, pricing information of loans.[163] Over the years, HMDA's reach and coverage have expanded.[164] For the purposes of this report, the most noteworthy amendments occurred in 1989 and 2002. In 1989, the Federal Reserve revised Regulation C to incorporate amendments in the Financial Institutions Reform, Recovery and Enforcement Act to include, *inter alia*, identification of race, sex, and income of loan applicants and borrowers and lenders were permitted to explain the basis for their lending decisions. In 2002, institutions were required to report rate-spread information on higher-priced loans, which is the

---

[156] *Id.* §§ 2608(b), 2617.

[157] Home Mortgage Disclosure Act, Pub. L. 94-200, 89 Stat. 1125 (codified at 12 U.S.C. § 2801(b) (1975)).

[158] National Credit Union Administration, Response to U. S. Commission on Civil Rights' Interrogatories and Document Requests, Response to Interrogatory Request.

[159] 12 U.S.C. § 2804 (2006).

[160] 12 C.F.R § 203 (2008).

[161] 12 U.S.C. § 2802 (2006).

[162] *Id.*

[163] *See* FFIEC, *Home Mortgage Disclosure Act: History of HMDA*, <http://www.ffiec.gov/HMDA/history2.htm> (last accessed April 24, 2009).

[164] *See id.*

first time that pricing data has been collected in HMDA data. In addition, HOEPA loans were identified and information on the type of property and lien-status of the loan were added[165]

Institutions must also maintain a loan application register with information from loans on which it reports. The reported information, in turn, must be disclosed in a statement by the Federal Financial Institutions Examination Council (FFIEC), which is disclosed to the public by the financial institution.[166]

HMDA provides the Federal Reserve with the general power to prescribe regulations necessary to carry out its purpose.[167] The Federal Reserve, OCC, OTS, NCUA, the FDIC, and HUD work together to develop the process for disclosing loan information to the public.[168] Enforcement of HMDA is shared by these same agencies.[169]

HMDA also requires the Federal Reserve, in consultation with the Secretary of HUD, to report annually to Congress the loan data collected.[170]

The Act provides that the above six agencies may enforce compliance under the Federal Credit Union Act and the Federal Deposit Insurance Act.[171] A depository institution that fails to comply with HMDA may face termination of its status as an insured depository institution,[172] and Regulation C also provides for civil and monetary penalties.[173] Moreover, violations of HMDA are also deemed violations of the Federal Credit Union Act and the Federal Deposit Insurance Act.[174]

In addition to the specific statutory and regulatory provisions cited above relative to home mortgage lending, the general prohibition against unfair or deceptive acts or practices found in Section 5 of the FTC Act also applies. All of the banking agencies have authority to enforce this law with respect to the institutions they supervise, although rulemaking authority is vested solely in the FRB, OTS, and NCUA.

7. Federal Housing Enterprises Financial Safety Act

The Federal Housing Enterprises Financial Safety Act of 1992 (FHEFSSA) reformed federal regulation of Fannie Mae and Freddie Mac. In addition to modifying their housing goals and providing for their

---

[165] See *id.* Even with these revisions, the scope of HMDA data has been criticized as being too narrow for purposes of fair lending enforcement. *See* U.S. Gov't Accountability Office, GAO-09-704, Fair Lending: Data Limitations and the Fragmented U.S. Financial Regulatory Structure Challenge Federal Oversight and Enforcement Efforts (July 2009).

[166] 12 C.F.R. § 203.5 (2008).

[167] 12 U.S.C. § 2804(a) (2006).

[168] *Id.* § 2803(h).

[169] *Id.* § 2804(b).

[170] *Id.* § 2807.

[171] *Id.* § 1818; i*d.* § 1751 et seq.

[172] *Id.* § 1818.

[173] 12 C.F.R. § 203.6(b) (2008).

[174] 12 U.S.C. § 2804(c) (2006).

monitoring as discussed above, FHEFSSA also contains several provisions relating to fair lending enforcement. Although the Housing and Economic Recovery Act of 2008 amended FHEFSSA to transfer various GSE oversight functions from HUD to the Federal Housing Finance Agency, HUD retained responsibility for administering FHEFSSA's fair lending provisions.

With regard to fair lending, FHEFSSA requires that HUD-issued regulations prohibit Fannie Mae and Freddie Mac from discriminating in their mortgage purchases and mandates that HUD "periodically review and comment on the underwriting and appraisal guidelines of each GSE to ensure that such guidelines are consistent with the Fair Housing Act and [FHEFSSA]."[175] FHEFSSA and HUD's regulations contain the same anti-discrimination provisions found in FHA, with age as an added protected class, and expressly prohibit "any consideration of the age or location of the dwelling or the age of the neighborhood or census tract where the dwelling is located in a manner that has a discriminatory effect."[176] FHEFSSA also provides HUD with the authority to request data from Fannie Mae and Freddie Mac to assist HUD in investigating whether a lender with which one of the GSEs does business has violated federal fair lending laws.[177] In addition, FHEFSSA directs Fannie Mae and Freddie Mac to undertake remedial actions against lenders that have been found to have violated federal fair lending laws.[178]

Additionally, the OCC, OTS, the FDIC, and the Federal Reserve enforce the requirements of RESPA with respect to institutions within their supervisory authority under 12 U.S.C. § 1818.

B. Federal Enforcement of FHA and ECOA

Enforcement of the Fair Housing Act falls within the ambit of HUD's Office of Fair Housing and Equal Opportunity and DOJ's Civil Rights Division's Housing and Civil Enforcement Section. In addition, OCC, OTS, the FDIC, and the Federal Reserve enforce the FHA with respect to institutions within their supervisory authority under 12 U.S.C. § 1818.

ECOA encompasses all types of loans, not just residential mortgage loans. Thus, enforcement of ECOA is shared by a variety of entities based on type of transaction and entity. For the purposes of this report in evaluating ECOA's protections to residential mortgage loan applicants and borrowers, DOJ, the Federal Reserve, NCUA, the FDIC, OCC, and OTS will be reviewed...

1. The Department of Housing and Urban Development

HUD is tasked with enforcing fair housing laws to prohibit discrimination in mortgage lending. Its primary tool in combating such discrimination is FHA.[179]

---

[175] *Id.* § 4545(1), (6).

[176] *Id.* § 4545(1); 24 C.F.R. § 81.42 (2008).

[177] 12 U.S.C. § 4545(2), (3) (2006); 24 C.F.R. § 81.44 (2008).

[178] 12 U.S.C. § 4545(5) (2006); 24 C.F.R. § 81.46 (2008).

[179] In addition to FHA, HUD administers and enforces the RESPA provisions applicable to all federally-related mortgage loans and administers the fair lending provisions of FHEFSSA.

Enforcement Efforts

Under FHA, HUD's Office of Fair Housing and Equal Opportunity (FHEO) investigates and prosecutes discrimination in home mortgage lending because of race, color, religion, national origin, sex, familial status, and disability.[180] In some instances, such discrimination may constitute what has been termed "predatory lending."[181] To enforce FHA, HUD has issued a number of memoranda of understanding with private entities. These include the Memorandum Regarding FFIEC Member Agency Notification in Fair Housing Act Complaints against Insured Financial Institutions; the Memorandum of Understanding Between and Among HUD and the National Association of Asian American Real Estate Professionals, the National Association of Hispanic Real Estate Professionals, the National Association of Real Estate Brokers, and the National Association of Realtors, and the Memorandum of Understanding Between Department of Housing and Urban Development and the FFIEC Member Agencies.[182]

Pursuant to FHA, HUD transmits to DOJ information regarding any case in which HUD has "reason to believe that a basis may exist for DOJ to file a pattern or practice claim."[183] Such cases may concern discriminatory financing, discrimination in making loans, discrimination in purchasing loans, discrimination in terms and conditions for making loans, and redlining. Between FY 1990 and January 2009, HUD referred 23 mortgage lending discrimination matters to DOJ.[184]

Complaint Processing

As previously discussed, prior to 1988, HUD could only investigate and conciliate complaints of housing discrimination.[185] With the adoption of the 1988 amendments to FHA, HUD was authorized to issue Charges of Discrimination and to adjudicate them before an Administrative Law Judge if none of the parties elected to proceed instead in federal District Court.[186] Such complaints concern discriminatory financing, discrimination in making loans, discrimination in purchasing loans, discrimination in terms and conditions for making loans, and redlining.

Between FYs 1990 and 2008, HUD closed 3,689 lending complaints for a variety of reasons ranging from procedural dismissals to a final determination on the merits.[187] In addition to the complaints processed internally by HUD, a large number of complaints are processed through HUD's Fair Housing

---

[180] HUD Response to Interrogatories and Document Requests, Interrogatory Request 12 at p. 4.

[181] *Id.*

[182] HUD Response to Interrogatories and Document Requests, Interrogatory Request 12 at p. 4.

[183] HUD Response to Interrogatories and Document Requests, Interrogatory Request 15 at p. 9 (citing 42 U.S.C. §3610(e)(2) (2006)). Such a case exists when a person or group of persons are "engaged in a pattern or practice of resistance to the full enjoyment of any of the rights granted by this subchapter [FHA], or that any group of persons has been denied any of the rights granted by this subchapter and such denial raises an issue of general public importance." 42 U.S.C. § 3614(a) (2006).

[184] HUD Response to Interrogatories and Document Requests, Interrogatory Request 14.

[185] U.S. Commission on Civil Rights, *The Fair Housing Amendments Act of 1988: The Enforcement Report*, September 1994, p. 5.

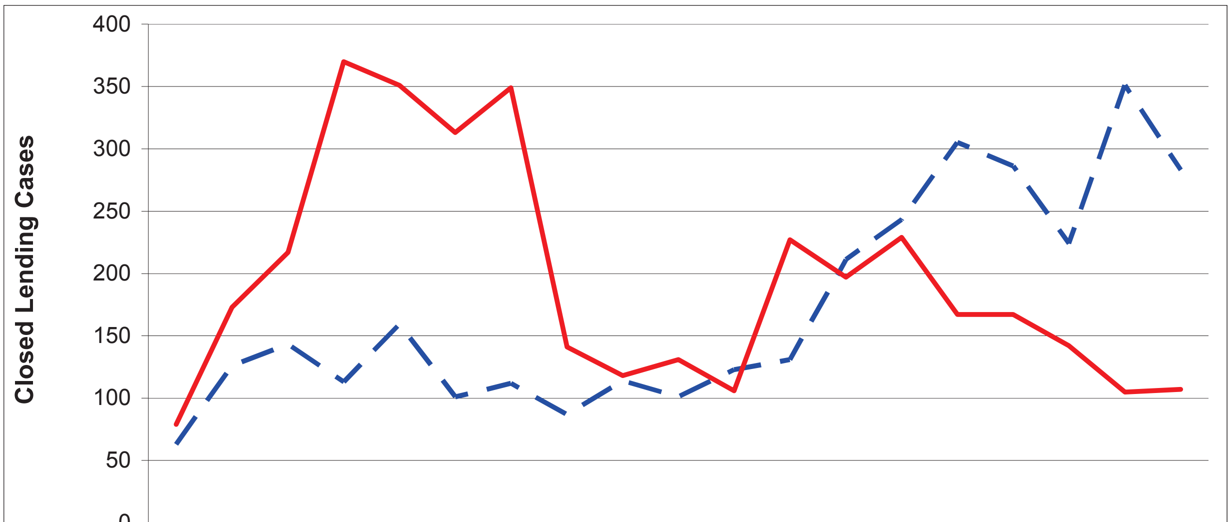
[186] *Id.* (citing Fair Housing Amendments Act of 1988 House Committee Report, 1988 U.S.C.C.A.N. 2173, 2178, p. 17). *See also* 42 U.S.C. §§ 3610 – 3613 (2006).

[187] HUD Response to Interrogatories and Document Requests, Interrogatory Request 13.

Assistance Program (FHAP). Under FHAP, HUD provides funding to state and local agencies that enforce fair housing laws substantially equivalent to FHA.[188] Between FYs 1990 and 2008, 3,276 lending complaints have been processed through FHAP agencies.

As reflected in Figure 4.3, the number of FHAP lending complaints closed increased substantially between 2004 and 2007. HUD closed 2 lending cases more in 2008 than in 2007 and FHAP closed 68 less lending complaints in 2008 than in the previous year.

Figure 4.3
Total Number of Closed HUD and FHAP Lending Complaints, 1990–2008



	1990	1991	1992	1993	1994	1995	1996	1997	1998	1999	2000	2001	2002	2003	2004	2005	2006	2007	2008
FHAP	63	126	143	113	159	101	112	87	114	101	123	131	211	243	305	286	224	351	283
HUD	79	173	217	370	351	313	349	141	118	131	106	227	197	229	167	167	142	105	107

Fiscal Year

Source: HUD Response to Interrogatories and Document Requests, Interrogatory Request 13.

Caption: During the 1990s, HUD closed significantly more lending complaints than FHAP. Since 2003, HUD has closed fewer and fewer lending complaints and by 2008, it closed 107 complaints. During this same period, FHAP has continuously closed a larger number of complaints than HUD. In 2008, FHAP closed 283 lending complaints.

Fair Lending Unit, Office of Systemic Investigations

In June 2007, HUD created the Fair Lending Unit, Office of Systemic Investigations in response to the high number of lending discrimination cases across the country. This office "investigates allegations of

[188] U.S. Department of Housing and Urban Development, *Fair Housing Assistance Program*, <http://www.hud.gov/offices/fheo/partners/FHAP/index.cfm> (last accessed Apr. 1, 2009).

discrimination in mortgage lending transactions."[189] In addition to investigating complaints of lending discrimination filed with HUD, this office also initiates its own investigations of potential violations of FHA.[190] This latter type of investigation, also known as Secretary-initiated investigations, has resulted in investigations against seven mortgage brokers or lenders, in which HUD used "information from a variety of sources, including Home Mortgage Disclosure Act data, to identify an investigation target."[191]

2. The Department of Justice

As part of DOJ's Civil Rights Division, the Housing and Civil Enforcement Section enforces FHA, ECOA, and other statutes involving discrimination in public accommodations, land use, public facilities, and service members' rights.[192] Of particular interest to this report is the Section's enforcement of FHA and ECOA, which covers forms of mortgage discrimination. DOJ reports that the bulk of its fair lending work has centered on three types of alleged discrimination: redlining, underwriting, and pricing, although DOJ also investigates predatory lending targeted at a protected class and discriminatory loan servicing.[193]

Compliance/Investigations/Litigation

FHA

In some instances, DOJ directly initiates litigation under FHA.[194] Through such lawsuits, DOJ can obtain monetary damages (actual and punitive) for individuals harmed by a defendant's discriminatory actions. Defendants may also be required to pay civil penalties to the government.[195] DOJ also may intervene in civil actions brought by individual plaintiffs when the Attorney General certifies that the case is of "general public importance."[196] Finally, DOJ initiates litigation on behalf of an individual complainant when the case is referred to the Housing and Civil Enforcement Section by HUD under 42 U.S.C. § 3612. This last enforcement mechanism is described in the "Complaints Processing" section, below.

---

[189] *Fair Housing/Office of Systemic Investigations Report for US Civil Rights Commission Request – February 2009*, HUD Response to Interrogatories and Document Requests, Interrogatory Request 13.

[190] *Id.*

[191] *Id.*

[192] DOJ, *Civil Rights Division Programs and Activities, Housing and Civil Enforcement Section*, <http://www.usdoj.gov/crt/activity.php#hce> (last accessed May 5, 2009).

[193] *Id.*

[194] 42 U.S.C. § 3614(a) (2006). The Attorney General may commence a civil action in U.S. district court whenever she has reason to believe "that any person or group of persons is engaged in a pattern or practice of resistance to the full enjoyment of any of the rights granted by [FHA] and such denial raises an issue of general public importance."

[195] *Id.* § 3614(d)(1)(C); DOJ, *Housing and Civil Enforcement Section*.

[196] 42 U.S.C. § 3613(e) (2006).

ECOA

DOJ may commence a civil action under ECOA whenever the Attorney General "has reason to believe that one or more creditors are engaged in a pattern or practice in violation of [ECOA]."[197] DOJ may also commence an ECOA action upon a referral from a bank regulatory agency.[198]

Processing of Complaints and Referrals

In the area of mortgage/lending practices, DOJ may receive referrals from HUD under FHA and from the FTC and the federal bank regulating agencies (OTS, OCC, the Federal Reserve, the FDIC, and NCUA) under ECOA.

FHA

As described previously, HUD investigates individual cases of housing discrimination under FHA. If HUD finds reasonable cause to believe that a discriminatory housing practice has occurred in a specific case, it refers the case to DOJ, at which point DOJ may initiate a civil action in any appropriate U.S. district court.[199] In the past 10 years, DOJ has received from HUD and filed in federal court between 12 and 31 "election" cases per year, but since 1999, none has involved fair lending issues. These cases are either handled directly by the Housing & Civil Enforcement Section of the Civil Rights Division or are handled by the appropriate United States Attorney's office working in coordination with the Civil Rights division. In addition, HUD refers subpoena enforcement matters and matters involving breach of conciliation agreements for enforcement by DOJ. Between 1999 and 2007, DOJ has handled six fair lending issues referred by HUD.

ECOA

Pursuant to ECOA, the federal bank regulators process individual complaints of discrimination. As with FHA, the agencies refer cases to DOJ when they find reasonable cause to believe that a pattern or practice of discrimination exists.[200]

At the behest of the Government Accountability Office, in 1996 DOJ provided guidance to the federal bank regulatory agencies on the characteristics of what constitutes a referable pattern or practice of discrimination. One purpose was to describe the distinction between those cases DOJ would pursue and those it would likely return to the referring agency.[201] As stated in DOJ's annual ECOA reports to Congress, as part of this guidance DOJ indicated that it would likely return cases in which

---

[197] 15 U.S.C. § 1691e(h) (2006).

[198] *Id.* § 1691e(g).

[199] 42 U.S.C. §§ 3610(e), 3614(a) (2006).

[200] Note that DOJ receives fair lending referrals on issues other than home mortgages, including credit card programs, loans to purchase automobiles, and loans for home improvement. Also note that violations of fair lending may also occur based on receipt of public assistance income or the applicant's good faith exercise of his or her rights under the Consumer Protection Act. 41 U.S.C. § 1691 (2006).

[201] DOJ, *The Attorney General's 2002 Annual Report to Congress Pursuant to the ECOA Amendments of 1996* (September 2003), <http:www.usdoj.gov/crt/housing/documents/ecoa2002.php> (last accessed Aug. 4, 2009) (hereinafter cited as DOJ, *2002 Annual Report*).

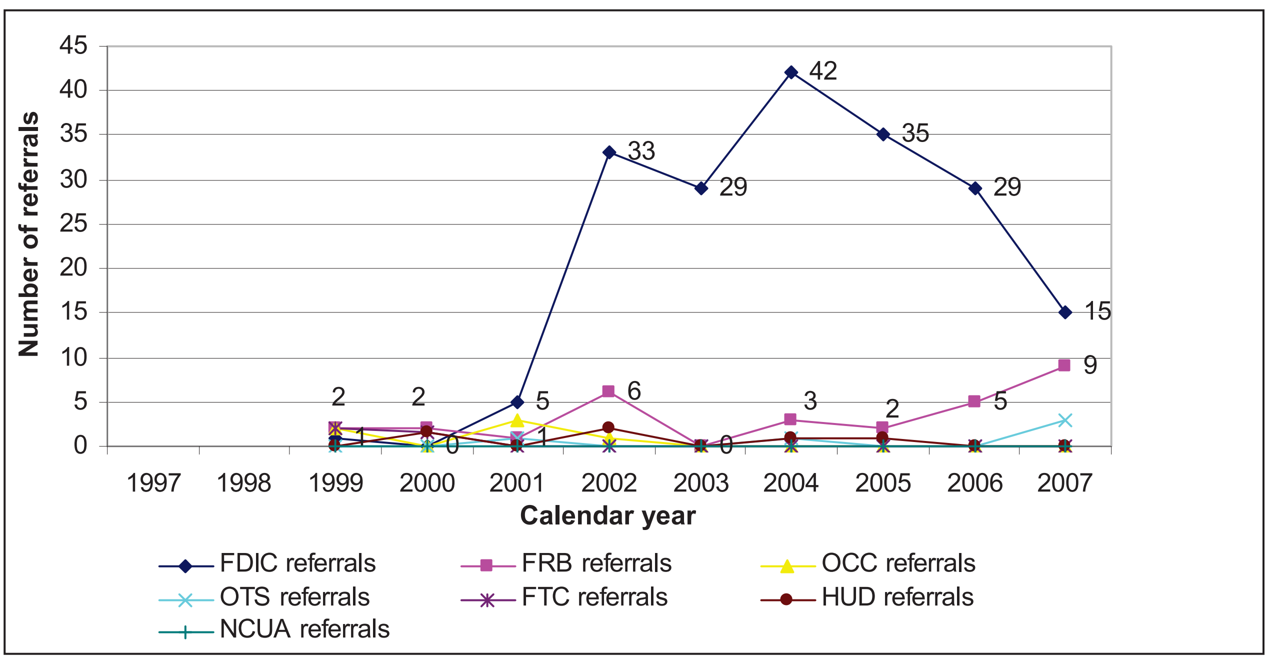
> (1) the practice has ceased and there is little chance that it will be repeated; and (2) the violation may have been accidental or arose from ignorance of the law's more technical requirements, such as spousal signature violations and minor price breaks for certain age groups not entitled to preferential treatment.[202]

These are the most common, but not the only circumstances under which DOJ would likely return a case to a bank regulatory agency.

When DOJ deems a referral appropriate for federal court litigation, it may bring a civil action for relief including actual and punitive damages and injunctive relief.[203] DOJ's annual ECOA reports to Congress describe for each year the referrals received and whether they were returned or retained for possible litigation.

As reflected in Figures 4.4 and 4.5, ECOA referrals have increased during the period of the housing boom. Figure 4.4 reflects the number of referrals made by each of the seven federal regulatory agencies. As said figure indicates, the great majority of such referrals have been made by the FDIC. Figure 4.5 reflects disposition of referrals to DOJ.

Figure 4.4
ECOA Referrals DOJ Received from Each of Seven Federal Regulatory Agencies, 1999–2007



Source: Compiled by U.S. Commission on Civil Rights using U.S. Department of Justice, Civil Rights Division's annual ECOA reports to Congress (1999 to 2007).

Caption: Of the ECOA referrals that DOJ received from other federal regulatory agencies, the greatest number came from FDIC, starting with 1 in 1999, then 5 in 2001, jumping to 33 in 2002, then hovering

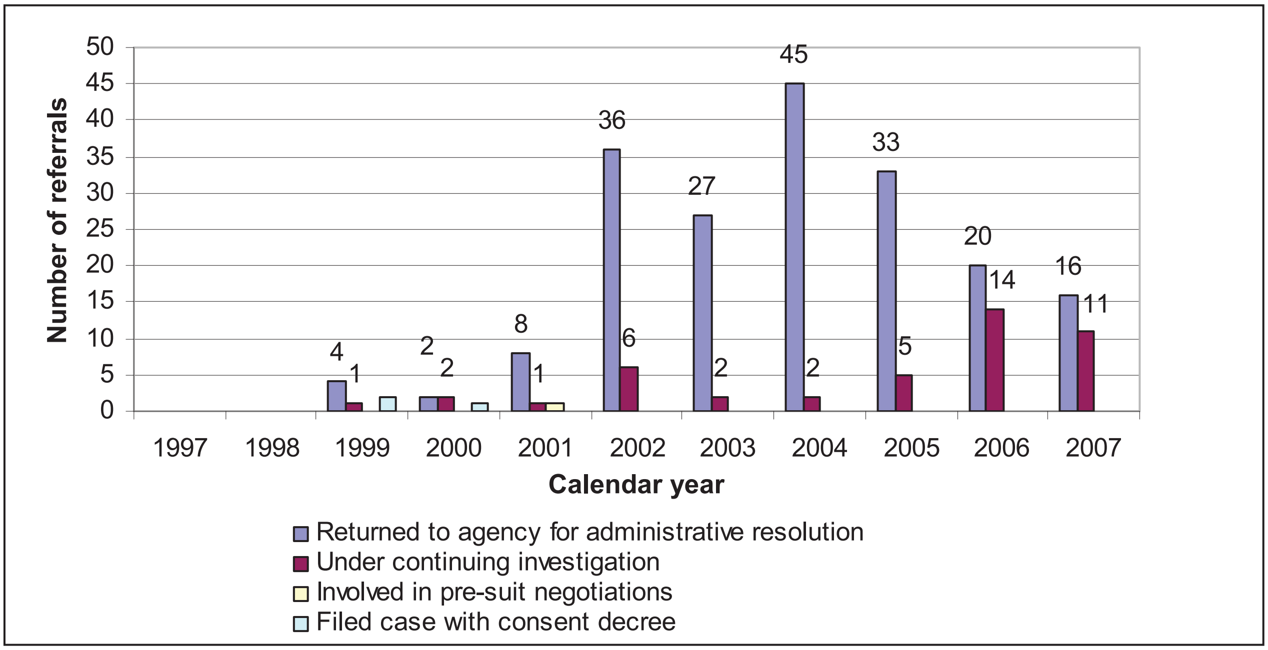
---

[202] *Id.*

[203] 41 U.S.C. § 1691e(h) (2006).

around 30 to 40 for the period from 2002 to 2006 and dropping to 15 in 2007. All other agencies had fewer than five referrals except for FRB in 2002 with 6, 2006 with 5, and 2007 with 9.

Figure 4.5
Dispositions of the Year's ECOA Referrals from Regulatory Agencies at Year's End, 1999–2007



Source: Compiled by U.S. Commission on Civil Rights using U.S. Department of Justice, Civil Rights Division's annual ECOA reports to Congress (1999 to 2007).

Caption: DOJ returned the vast majority of ECOA referrals from regulatory agencies to the referring agency for administrative resolution. In most years before 2006, DOJ retained only 1 or 2 referrals for continuing resolution, although it kept 5 or 6 in 2002 and 2005. In 2006 and 2007, DOJ retained 14 and 11 ECOA referrals for continuing investigations.

Of the 246 referrals reflected in the Housing Section's annual ECOA reports to Congress, between 1999 and 2007, only 17 were home mortgage matters involving claims of racial or national origin discrimination, less than 7 percent of the total.[204] These relevant referrals included:

- A 2002 HUD referral of an allegation that a Washington, D.C. area lender steered African-American and Hispanic borrowers to FHA-insured loan products and discriminated in the terms and conditions of the loans. The complaint's evidence was based primarily on testing conducted nearly five years before the time of referral. DOJ concluded that the evidence was insufficient to warrant an enforcement action and returned the matter to HUD.[205]

---

[204] Of these 17 referred cases, the ECOA reports indicate that three were returned to the agencies for administrative enforcement during the reporting year.

[205] DOJ, *2002 Annual Report*.

- Seven allegations that lenders discriminated in the pricing of mortgages: two FDIC referrals in 2006 and one in 2007; two OTS referrals in 2007; and two FRB referrals in 2007. The first five of these were on the basis of race; the last two were on race and/or national origin.[206]
- A 2006 FRB referral concerned redlining. The complaint alleged that a mortgage company excluded certain neighborhoods from the bank's mortgage lending activities on the basis of race.[207]

In addition to processing referrals, conducting investigations, and initiating litigation, DOJ's Housing Section coordinates activities with other federal agencies to bring about better fair lending enforcement.[208] For example, it works with the Interagency Task Force on Fair Lending, a group currently chaired by the OCC.[209]

The task force agencies have jointly published and distributed consumer brochures on shopping for the best mortgage price[210] and the pitfalls of borrowing against your home, the potential of high-cost home

---

[206] DOJ, *The Attorney General's 2006 Annual Report to Congress Pursuant to the ECOA Amendments of 1976 (*March 2007), <http://www.usdoj.gov/crt/housing/fairhousing/reports_congress.htm> (last accessed Apr. 3, 2009) (hereinafter cited as DOJ, *2006 Annual Report*); DOJ, *The Attorney General's 2007 Annual Report to Congress Pursuant to the ECOA Amendments of 1976 (*April 2008), <http://www.usdoj.gov/crt/housing/fairhousing/reports_congress.htm> (last accessed Apr. 3, 2009) (hereinafter cited as DOJ, *2007 Annual Report*).

[207] Also included amongst the 17 referred complaints: 1) a 2000 FTC referral concerning allegations of a lender charging African Americans higher points and fees in connection with home mortgages; 2) a 2000 HUD referral alleging that a subprime lender engaged in a pattern or practice or disparate treatment of African American borrowers in the pricing of loans; 3) a 2002 HUD referral alleging that Hispanics are charged higher interest rates for loans to purchase mobile homes; 4) two HUD referrals from 2004 and 2005 alleging that a lender discriminated against African Americans by targeting them for "predatory loans" with high fees and interest rates; 5) a 2007 FRB referral of an allegation that a bank had implemented two criteria as part of its underwriting policies that appeared to be discriminatory on the basis of race or national origin. (After reviewing the evidence, DOJ returned the matter for administrative resolution because "the bank revised its lending policy and expressed willingness to take appropriate corrective action for any persons who were aggrieved by the discriminatory policy."). DOJ, *The Attorney General's 2000 Annual Report to Congress Pursuant to the ECOA Amendments of 1976* (April 2001), <http://www.usdoj.gov/crt/housing/documents/ecoa2000.php> (last accessed Feb. 18, 2009) (hereinafter cited as DOJ, *2000 Annual Report*); DOJ, *The Attorney General's 2001 Annual Report to Congress Pursuant to the ECOA Amendments of 1976* (March 2002), <http://www.usdoj.gov/crt/housing/documents/ecoa2001.php> (last accessed Feb. 18, 2009) (hereinafter cited as DOJ, *2001 Annual Report*); DOJ, *2002 Annual Report*; DOJ, *The Attorney General's 2003 Annual Report to Congress Pursuant to the ECOA Amendments of 1976* (June 2004), <http://www.usdoj.gov/crt/housing/documents/ecoa2003.php> (last accessed Feb. 18, 2009) (hereinafter cited as DOJ, *2003 Annual Report*); DOJ, *The Attorney General's 2004 Annual Report to Congress Pursuant to the ECOA Amendments of 1976* (March 2005), <http://www.usdoj.gov/crt/housing/documents/ecoa2004.php> (last accessed Feb. 18, 2009) (hereinafter cited as DOJ, *2004 Annual Report*); DOJ, *The Attorney General's 2005 Annual Report to Congress Pursuant to the ECOA Amendments of 1976* (March 2006), <http://www.usdoj.gov/crt/housing/documents/ecoa2005.php> (last accessed Feb. 18, 2009) (hereinafter cited as DOJ, *2005 Annual Report*); DOJ, *2006 Annual Report;* DOJ, *2007 Annual Report*.

[208] DOJ, *The Attorney General's 1999 Annual Report to Congress Pursuant to the ECOA Amendments of 1976 (*March 2000), <http://www.usdoj.gov/crt/housing/documents/ecoa1999.php> (last accessed Feb. 18, 2009) (hereinafter cited as DOJ, *1999 Annual Report*); DOJ, *2006 Annual Report*; DOJ, *2007 Annual Report*.

[209] DOJ, *1999 Annual Report*; DOJ, *2000 Annual Report*; DOJ, *2001 Annual Report*; DOJ, *2002 Annual* Report; DOJ, *2003 Annual Report*; DOJ, *2004 Annual Report*; DOJ, *2005 Annual Report*; DOJ, *2006 Annual Report*; DOJ, *2007 Annual Report*.

[210] DOJ, *1999 Annual Report* (citing Federal Reserve Board, *Looking for the Best Mortgage: Shop, Compare, Negotiate*, <http://www.federalreserve.gov/pubs/mortgage/mortb_1.htm> (last accessed August 3, 2009).

loans, and tips for getting the best financing.[211] These brochures are available in English and Spanish. From 1999 to 2001, the task force discussed predatory lending issues with the goal of developing a policy statement on the currently available enforcement options that agencies can take under existing law.[212]

3. The Federal Trade Commission

The FTC divides its work among three bureaus: (1) the Bureau of Consumer Protection (BCP) protects consumers from unfair or deceptive practices in the marketplace by enforcing consumer protection laws and trade regulation rules; (2) the Bureau of Competition prevents anticompetitive business practices by overseeing mergers and enforcing antitrust laws; and (3) the Bureau of Economics evaluates and analyzes the activities of the FTC and their effect in the marketplace. The mortgage lending and related issues at issue in this report fall to the BCP.[213]

Among the laws the agency enforces are TILA, the Fair Credit Billing Act, the Fair Credit Reporting Act, the Home Equity Loan Consumer Protection Act, HOEPA, and the Fair and Accurate Credit Transactions Act and the Fair Debt Collection Practices Act.[214]

Unlike other financial regulatory agencies, the FTC does not conduct compliance examinations, focusing instead on law enforcement activities.[215] It also does not resolve individual consumer complaints, although it does collect such information to determine patterns of wrongdoing, which can lead to investigations and prosecutions.[216]

The FTC performs statistical analysis of the data financial companies reported pursuant to HMDA to investigate claims of discrimination.[217] It uses the HMDA data as a screening or targeting tool.[218] HMDA data include pricing and loan application data, but lack key information lenders used to evaluate the risk of a loan, such as borrower credit scores, loan-to-value ratios, debt-to-income ratios, loan type, and length of loan. For this reason, HMDA data alone are insufficient to establish a law violation.[219]

---

[211] DOJ, *2003 Annual Report.* The brochure is *Putting Your Home on the Loan Line is Risky Business*.

[212] DOJ, *1999 Annual Report*; DOJ, *2000 Annual Report*; DOJ, *2001 Annual Report*.

[213] Federal Trade Commission, *A Guide to the Federal Trade Commission*, available at, <http://www.ftc.gov/bcp/edu/pubs/consumer/general/gen03.shtm> (last accessed Aug. 4, 2009).

[214] Federal Trade Commission, *Legal Resources—Statutes Relating to Consumer Protection Mission,* <http://www.ftc.gov/ogc/stat3.shtm> (last accessed March 31, 2009).

[215] Prepared Statement of the Federal Trade Commission on *Home Mortgage Disclosure Act Data and FTC Lending Enforcement* before the House Committee on Financial Services Subcommittee on Oversight and Investigations (July 25, 2007), p. 2 (hereinafter cited as FTC Statement, *Lending Enforcement*).

[216] Federal Trade Commission, *Before You Submit a Complaint,* <http://www.ftccomplaintassistant.gov> (last accessed Dec. 9, 2008).

[217] FTC Statement, *Consumer Protections* at p. 8.

[218] FTC Statement, *Lending Enforcement* at p. 7.

[219] *Id.* at pp. 7–8.

According to the FTC, several non-public investigations of mortgage originators for possible violations of fair lending laws were in progress as of April 2008.[220]

Enforcement Efforts

Since the enactment of ECOA, the FTC has initiated more than three dozen cases against subprime lenders, major non-mortgage creditors, and smaller finance companies under the statute.[221] In about two dozen of these cases it alleged substantive discrimination on the basis of race, marital status, sex, age, and the receipt of public assistance.[222] Examples include:

- In May 2009, the FTC sued Golden Empire Mortgage, Inc. and its owner, Howard D. Kootstra. The FTC alleges that the defendants violated ECOA by charging Hispanic borrowers higher loan prices than non-Hispanic whites. The FTC has alleged that the price disparities were substantial, statistically significant, and could not be explained by factors related to underwriting risk or credit characteristics of the mortgage applicants.[223]

- In December 2008, the FTC settled with Gateway Funding Diversified Mortgage Services, L.P., and its general partner, Gateway Funding Inc. ("Gateway"). The Commission alleged that Gateway violated ECOA because African-American and Hispanic consumers were charged higher prices for mortgage loans than non-Hispanic white consumers.[224]

- In 2000 the FTC joined with DOJ and HUD to secure a settlement with Delta Funding Corp., a national subprime mortgage lender, to resolve alleged violations of ECOA, HOEPA, and RESPA.[225]
- The FTC filed a complaint against a large subprime mortgage lender, Associates First Capital Corporation and Associates Corporation of North America (the Associates),[226] alleging that it used false and misleading statements to market subprime loans. In particular, the FTC alleged that the Associates informed consumers that they could save money when consolidating their

---

[220] FTC Statement, *Consumer Protections* at pp. 8–9.

[221] *Id.* at p. 8.

[222] *Id.*

[223] E-mail from Katherine Worthman, Division of Financial Practices, Federal Trade Commission, to U.S. Commission on Civil Rights (July 8, 2009, 6:17 p.m. EDT) (on file with the Commission).

[224] Prepared Statement of the Federal Trade Commission on *Consumer Credit and Debt: The Role of the Federal Trade Commission in Protecting the Public* before the House Committee on Energy and Commerce Subcommittee on Commerce, Trade, and Consumer Protection (March 24, 2009), p. 12.

[225] FTC Statement, Lending Enforcement at pp. 10–11 (citing *United States v. Delta Funding Corp*., No. 00-1871 (E.D.N.Y. 2000)). According to the FTC, the complaint alleged that Delta had engaged in a pattern or practice of asset-based lending and other practices in violation of HOEPA; that higher broker fees were charged to African-American females than to White males in violation of the ECOA and the Fair Housing Act, 42 U.S.C. §§ 3601-3619, and that few or no services were performed in exchange for certain broker charges in violation of the Real Estate Settlement Procedures Act, 12 U.S.C. § 2607.

[226] FTC Statement, *Consumer Protections* at p. 5 (citing *FTC v. Associates First Capital Corp.,* No. 01-00606 (N.D. Ga. 2001)).

> existing debts. However, the FTC said these "saving claims" did not take into account loan fees and closing costs that the Associates typically added to consumers' loan amounts.[227] The FTC further alleged that the Associates failed to reveal that, for certain of its loans, consumers would pay only interest but still would owe the entire principal amount in a "balloon" payment at the end of the loan term. The FTC also alleged the Associates' practice of not disclosing to consumers inclusion of single-premium credit insurance in loans was deceptive. The Associates paid a record $215 million in consumer redress to settle the allegations according to the agency.[228]

4. The Board of Governors of the Federal Reserve System

The Federal Reserve System is the central banking system of the United States, created in 1913 through the Federal Reserve Act.[229] The system comprises of twelve regional federal reserve districts and the Board.[230] Among the variety of duties the Federal Reserve performs, its role in HMDA data collection and fair lending examinations is particularly noteworthy here.

Assisting and Advising Other Federal Agencies in Their Enforcement Activities

The Federal Reserve regards HMDA data as a useful tool that can be used by federal and state agencies to facilitate fair lending enforcement. The Federal Reserve has a special role in maintaining and expanding these data, making them available for other federal agencies' analyses, and offering advice on their proper use.[231] In explaining the system's usefulness before the 2004 expansion in information, the Federal Reserve staff state:

> For some time, the Federal Reserve has been using a statistical analysis system that relies on the HMDA data to help assess fair lending compliance by high-volume mortgage lenders. The system identifies which supervised institutions and which loan products and geographic markets show meaningful differences in the denial rates of loan applications by the race, ethnicity, or sex of the borrower and thus warrant greater supervisory attention.[232]

The 2004 revisions in the collection of HMDA data allowed more precise differentiation among loan products and provided new loan pricing information that agencies could review for differences across groups in the incidence of higher-priced lending and for broader patterns indicating fair lending issues.[233]

---

[227] *Id.* at pp. 5–6.

[228] *Id.* at p. 5 (citing *FTC v. Associates First Capital Corp.,* No. 01-00606 (N.D. Ga. 2001)).

[229] Federal Reserve Board, *FAQs: Federal Reserve System*, <http://www.federalreserve.gov/generalinfo/faq/faqfrs.htm> (last accessed Aug. 4, 2009).

[230] *Id.*

[231] Robert B. Avery, Glenn B. Canner, and Robert E. Cook, Federal Reserve Board, *New Information Reported under HMDA and Its Application in Fair Lending Enforcement*, *FED. RES. BULL.,* Summer 2005, at p. 387.

[232] *Id.*

[233] *Id.*

The Federal Reserve staff has also warned of the limitations of HMDA data:

> We emphasize that the Federal Reserve's statistical analysis system is only a screening tool. The HMDA data alone, no matter how much they are manipulated, cannot be used to conclude whether a particular applicant was treated adversely on the basis of a prohibited factor regarding either the disposition of the application or the pricing of the loan. The data reveal little about an individual's financial circumstances and nothing about the condition or value of the property offered as collateral. Furthermore, the data reveal nothing about the underwriting standards used by a lender to assess the creditworthiness of an individual or to set loan prices. Moreover, the data do not reveal how a lender's credit decisions relate to its overall business strategy. For example, the data do not account for the possibility that an institution's outreach efforts may attract a larger proportion of applicants with weaker credit profiles than do other institutions. Consequently, the data do not provide a final basis on which to draw conclusions regarding either the existence or the absence of fair lending violations.[234]

In the Federal Reserve's own bank supervisory process, the agency uses statistical analysis

> to identify financial institutions and their specific products that warrant closer review for fair lending concerns. Examiners familiar with the procedures and products of a given institution conduct the analysis and tailor it to the specific circumstances relevant to the institution….[235]

If the Federal Reserve targets an institution for more intensive review, the examiner may solicit more information from the institution regarding its lending and underwriting procedures; gather additional loan-level data, such as credit scores and loan-to-value ratios; perform detailed reviews of loan-file data; and/or conduct interviews with current or past bank personnel or borrowers. These follow-up procedures may be integrated into the normal consumer examination cycle or become a special review of fair lending compliance.[236]

In 2005, the Federal Reserve reported sharing its screening procedures with other agencies so that, if they chose, they could integrate them into their supervisory programs. For example, the Federal Reserve reviewed 2004 HMDA data by other agencies for this purpose. It also responded to agency requests for additional, more detailed analysis of individual institutions that were of concern to the other federal entities.[237]

Finally, for agencies that evaluate compliance with HOEPA, the HMDA data that were expanded in 2004 offered the first opportunity to identify readily which lenders extend home loans that are subject to that law and to measure the extent of these institutions' involvement in such lending. HOEPA examiners can use the expanded data to efficiently select samples of loan files for

---

[234] *Id.* at pp. 389–90.

[235] *Id.* at p. 390.

[236] *Id.*

[237] *Id.* at pp. 390–91.

review and examine patterns of HOEPA-related lending across borrowers and neighborhoods, arrayed by their racial and ethnic profiles. The Federal Reserve may screen for potentially unaffordable HOEPA loans given an applicant's income and estimated monthly loan payments, or calculate differences across racial and ethnic groups in the incidence of HOEPA lending. Thus, HMDA analysis may reveal fair lending issues.[238]

Fair Lending Examinations

The Federal Reserve conducts examinations using the Interagency Fair Lending Examination Procedures. Examiners review information related to the institution, its credit products, and the markets it serves; assess fair lending risk across business lines; evaluate the bank's fair lending compliance program, and determine whether violations have occurred.[239]

The agency performs fair lending reviews both within the context of its normal supervisory cycle for consumer compliance examination and when concerns about fair lending arise outside the usual cycle (such as from consumer complaints or based on the HMDA screening process described below).[240]

When the Federal Reserve examiners find fair lending violations, the agency refers matters that suggest a pattern or practice of discrimination under ECOA to DOJ, and, for more isolated instances, direct the institution to correct the violations and improve its fair lending compliance, as appropriate.[241]

The Federal Reserve referred eight matters to DOJ in 2007 and three in 2008.[242] Many of these involved gender or marital status discrimination. Three of the 2007 matters concerned racial discrimination in obtaining home mortgages. Two of them involved mortgage pricing discrimination by race and ethnicity, where Hispanics and African-Americans paid higher mortgage prices across several metropolitan areas. A third case arose from restrictions on row house lending that discriminated by race and constraints on lending on Native American lands.[243]

Over time, the Federal Reserve has relied upon the statistical analysis of electronic data (i.e., HMDA data enhanced with other relevant fields) to increase the efficacy and efficiency of its fair lending reviews, including examinations of small lenders. It has conducted more reviews of lending policies for disparate impact, maintained a focus on loan pricing, and broadened its definition of steering. As some lenders have implemented declining market restrictions, the agency has emphasized the importance of analyzing these restrictions for fair lending risk. Also, it is concerned about the relationship between

---

[238] *Id.* at p. 392.

[239] Federal Reserve Board, *Fair Lending Enforcement Process*, Briefing by Federal Reserve Board Staff for the U. S. Commission on Civil Rights, Jan. 28, 2009, p. 3.

[240] *Id.* at p. 4.

[241] *Id.* at p. 5.

[242] Federal Reserve Board, *Fair Lending Enforcement Process*, Briefing by Federal Reserve Board Staff for the United States Commission on Civil Rights, Jan. 28, 2009, pp. 7, 8.

[243] One 2007 matter concerned racial discrimination in auto loan pricing. *See* Federal Reserve Board, *Fair Lending Enforcement Process,* Briefing by Federal Reserve Board Staff for the U.S. Commission on Civil Rights, Jan. 28, 2009, pp. 4, 6–7, 14.

tightening underwriting standards and access to credit, as well as the interplay between fair lending and responsible lending.[244]

5. The National Credit Union Administration

The Federal Credit Union Act, enacted in 1934, authorized the formation of federally-chartered credit unions in all states and established the Bureau of Federal Credit Unions. The Bureau became an independent financial federal regulatory agency in 1970 with the creation of the NCUA to charter and supervise federal credit unions.[245] The National Credit Union Share Insurance Fund (NCUSIF) was established at the same time to insure federal and state-chartered credit union deposits. In 1977, legislative action expanded services available to credit union members, including issuance of share certificates and origination of mortgage loans.[246] Currently, approximately 7,735 federally-insured credit unions serve 89.2 million members with $724 billion on deposit.[247]

NCUA enforces many consumer protection and financial protection laws and regulations,[248] including the key laws designed to prevent discrimination, namely FHA and ECOA. [249] All credit unions report their members' loan data in accordance with HMDA to the Federal Reserve.[250]

Compliance Examinations

As discussed previously, Regulation B defines and details the enforcement powers under ECOA as well as its examination and supervision process. [251] While the process is independent of the Federal Financial Institutions Examination Council (FFIEC), the agency relies on guidance collaboratively developed with other Council members.[252] According to NCUA, two objectives drive the examination and supervision process: (1) determining whether federal credit unions discriminate on any of the bases prohibited by

---

[244] *Id.* at pp. 15–18.

[245] Federal Credit Union Act, 12 U.S.C. § 1751 et seq. (2006).

[246] National Credit Union Administration, *About NCUA and NCUA History*, <http://www.ncua.govAboutNCUA/Index.htm> (last accessed Nov. 17, 2008).

[247] E-mail from Ross P. Kendall, Trial Attorney, Office of the General Counsel, National Credit Union Administration, to David P. Blackwood, General Counsel, U.S. Commission on Civil Rights (July 7, 2009, 3:45p.m. EDT) (on file with the Commission).

[248] National Credit Union Administration, *Regulations, Legal Opinions and Law* <http://www.ncua.gov/RegulationsOpinionsLaws/index.htm> (last accessed Nov. 18, 2008); National Credit Union Administration, *Laws and Enforcement Authorities for Credit Unions*, <http://www.ncua.gov/RegulationsOpinions/Laws/LawEnforcementAuthorities.pdf> (last accessed Nov. 18, 2008).

[249] NCUA Response to Interrogatories and Document Requests, Interrogatory Request 6 at p. 6.

[250] E-mail from Ross P. Kendall, Trial Attorney, Office of the General Counsel, National Credit Union Administration, to David P. Blackwood, General Counsel, U.S. Commission on Civil Rights (July 7, 2009, 3:45p.m. EDT) (on file with the Commission).

[251] NCUA Response to Interrogatories and Document Requests, Interrogatory Request 6 at p. 5.

[252] NCUA Response to Interrogatories and Document Requests, Interrogatory Request 17 at p. 15. The most recent guidance, Interagency Fair Lending Guidelines, and related Appendix are available at the FFIEC Web site, <http://www.ffiec.gov/PDF/fairlend.pdf> and <http://www.ffiec.gov/PDF/fairappx.pdf>, respectively.

ECOA in the granting of credit; and (2) determining whether federal credit unions have adequate procedures in place for complying with the requirements of ECOA.[253]

NCUA identifies seven risk areas: credit, interest rate, liquidity, transaction, compliance, strategic, and reputation.[254] Under a risk-focused examination program, examiners assign to each risk a rating of high, medium, or low. Examiners then develop the scope for each examination or supervision contact based upon a credit union's individual risk factors.

NCUA also conducts fair lending examinations to assess Regulation B compliance in greater detail. The agency determines the number of credit unions it will examine each year depending on the availability of resources. Regional directors then select a pool of credit unions based on a variety of considerations, including adverse HMDA data over a multi-year period and previous fair-lending examination findings.[255]

With respect to federally insured state-chartered credit unions, NCUA's focus is addressing safety and soundness concerns that might present a risk to the NCUSIF. NCUA generally defers to state regulators with regard to consumer violations, but will become actively involved with fair lending issues at a federally insured state-chartered credit union if such issues expose the NCUSIF to risk. NCUA also refers matters to DOJ and HUD as appropriate.[256]

Complaints Processing

In 2005, NCUA contemplated referral action in a case of apparent disparate treatment of Hispanic and non-Hispanic applicants by a state-chartered credit union. NCUA ultimately decided against referring the case to DOJ after the management of the state-chartered credit union corrected concerns about disparate treatment and responded to the agency's supervisory process by strengthening lending controls.[257] With the exception of the above-mentioned episode, from FY 1990 to the present, it has resolved fair-lending violation issues through routine examination and supervisory process.[258]

---

[253] NCUA Response to Interrogatories and Document Requests, Interrogatory Request 16 at p. 14.

[254] NCUA stated that it identified these seven risks in NCUA Letter to Federal Credit Unions 02-FCU-09. *Id.* at p. 14 n.4.

[255] NCUA Response to Interrogatories and Document Requests, Interrogatory Request 16 at p. 14.

[256] *Id.* at p. 15.

[257] NCUA Response to Interrogatories and Document Requests, Interrogatory Request 7 at p. 6.

[258] *Id.*

NCUA provides consumers with the information necessary to submit complaints via e-mail, telephone, and letter.[259] Consumers whose complaint involves a state-chartered credit union are referred by NCUA personnel to the appropriate state regulatory authority for appropriate action.[260] Federal credit unions have supervisory committees responsible for investigating member complaints.[261]

According to the agency, on notification of a complaint, supervisory committees will conduct an investigation, determine the appropriate course of action, and report back to NCUA. The agency will review all complaints and follow up when necessary. All violations are recorded internally and reported to the Federal Reserve Board annually.[262]

NCUA's review of responses to complainants indicated that the supervisory committees are meeting their mandates. Should the agency determine otherwise, it will intervene by assigning an examiner to investigate and remedy the situation. If this proves to be unsuccessful, NCUA may issue letters of understanding and agreement, cease and desist orders, and/or assess civil money penalties.[263]

If not satisfied with NCUA's solution, a complainant may contact the NCUA Ombudsman, who is independent of the operational programs of the agency. The Ombudsman assists by identifying options and recommending actions, but may not decide issues or advocate positions of any party.[264]

According to NCUA, the overwhelming majority of member complaints result from a misunderstanding of federal credit union policies or poor communication between the complainant and the federal credit union. As a result, almost all complaints are resolved informally. NCUA member complaints have not led to enforcement actions related to minority homeownership, predatory lending, and/or home mortgage lending. NCUA relies on data on complaints and actions taken to identify federal credit unions at potential risk of lawsuits.[265] It does not collect data about lawsuits filed against federal credit unions nor does it maintain a centralized complaint database.[266]

---

[259] NCUA Response to Interrogatories and Document Requests, Interrogatory Request 4 at p. 2.

[260] E-mail from Ross P. Kendall, Trial Attorney, Office of the General Counsel, National Credit Union Administration, to David P. Blackwood, General Counsel, U.S. Commission on Civil Rights (July 7, 2009, 3:45p.m. EDT) (on file with the Commission).

[261] National Credit Union Administration, *Supervisory Committee Guide for Federal Credit Unions*, NCUA Publication No. 8023, Section 4.12, <www.NCUA.gov> (last accessed July 21, 2009).

[262] NCUA Response to Interrogatories and Document Requests, Interrogatory Request 4 at p. 2.

[263] *Id.* at p. 4.

[264] *Id.*

[265] *Id.*

[266] *Id.*

6. The Federal Deposit Insurance Corporation

The FDIC was established in 1933 as an independent agency in response to bank failures during the Great Depression.[267] While a significant component of its mission is to provide insurance to depositors in banks and thrift institutions, the FDIC supervises state chartered banks that are not members of the Federal Reserve System. The FDIC directly examines and supervises approximately 5,160 banks and savings banks, more than half of the total number of institutions in the banking system.[268] ECOA compliance is among the various laws it enforces[269]

Compliance Examinations

As the primary regulator of state-chartered banks that are not members of the Federal Reserve, the FDIC conducts compliance examinations, visitations and investigations to ensure that state-chartered nonmember institutions adhere to federal consumer protection laws, fair lending statutes and regulations, HMDA and CRA. The FDIC performs compliance examinations to assess the quality of an FDIC-supervised institution's compliance management system, reviews compliance with relevant laws and regulations, and initiates administrative enforcement action when elements of an institution's compliance management system are deficient or when major violations of law are discovered.[270] Visitations are used to review the compliance soundness of newly-chartered institutions and institutions converting to state non-member status.[271] The FDIC also uses visitations to assess progress on corrective actions or to ensure compliance with an enforcement action during the interval between compliance examinations.[272] The FDIC conducts investigations to follow up on consumer inquiries or complaints, including those regarding fair lending.

While most violations are corrected by the institution as part of the examination process, the more serious issues, including discrimination, normally result in formal or informal enforcement actions.[273] The FDIC defines its informal actions as voluntary commitments made by the Board of Directors or trustees of a financial institution, that are designed to resolve identified deficiencies and ensure compliance with federal and state banking laws and regulations.[274] Informal actions are not publicly disclosed.[275] Formal enforcement actions are made pursuant to Section 8 of the Federal Deposit

---

[267] Federal Deposit Insurance Corporation, *Who is the FDIC?*, <http://www.fdic.gov/about/learn/symbol/index.html> (last accessed Apr. 22, 2009).

[268] *Id.*

[269] Federal Deposit Insurance Corporation, Response to U.S. Commission on Civil Rights' Interrogatories and Document Requests, Response to Interrogatory Request 4 at pp. 3–4.

[270] FDIC Response to Interrogatories, Response to Interrogatory Request 10 at p. 10. A detailed description of the examination process can be found at <http://www.fdic.gov/regulatins/compliance/handbook/compmanual.pdf>.

[271] FDIC Response to Interrogatories and Document Requests, Interrogatory Request 9 at p. 9.

[272] *Id.* at pp. 9–10.

[273] FDIC Response to Interrogatories and Document Requests, Interrogatory Request 5 at p. 6.

[274] *Id.*

[275] *Id.*

Insurance Act.[276] In addition, if the FDIC has reason to believe that a pattern or practice of fair lending violations has occurred, the FDIC must make a referral to DOJ for enforcement.

Complaint Processing

The consumer complaint process at the FDIC is handled by the Consumer Response Center (CRC) headquartered in Kansas City, Missouri, and the Consumer Affairs Section located in Washington, D.C. CRC staff are responsible for investigating all consumer complaints and responding to consumer inquiries. Staff are located in almost all regional and area offices. When a consumer complaint is received, it is logged into the FDIC's consumer complaint and inquiry database, which captures data about each complaint and inquiry the FDIC receives, as well as supporting documents for a given case.[277] According to the FDIC, it codes complaints based on the consumer's allegation, and not on whether the complaint is ultimately found to have merit.[278] The FDIC indicates that it does not capture information about the specific race or ethnicity of the consumer.[279]

The FDIC indicates that its record retention policy for consumer complaints is five years. As reflected in Figure 4.6 between 2003 and March 2008, the FDIC received 254 complaints alleging discrimination based on race, color and national origin. Of the 254 complaints received, only 45 complaints, or 17.7 percent, alleged discrimination in the area of home mortgage lending. As reflected in Figure 4.6, in 2003, there were 11 consumer complaints alleging discrimination in mortgage lending based on race, color and national origin. For 2003, none of these allegations was based on national origin. The number of complaints filed alleging mortgage lending discrimination decreased to 6 in 2004, and in 2007 that number had increased to 8 complaints. As of 2008, 8 complaints alleging mortgage lending discrimination had already been filed, with 1 complaint based on national origin and the remaining 7 based on race and/or color.

According to data the FDIC provided, less than one percent of the total number of complaints it received between 2003 and 2008 alleged mortgage discrimination.[280]

---

[276] *Id.*

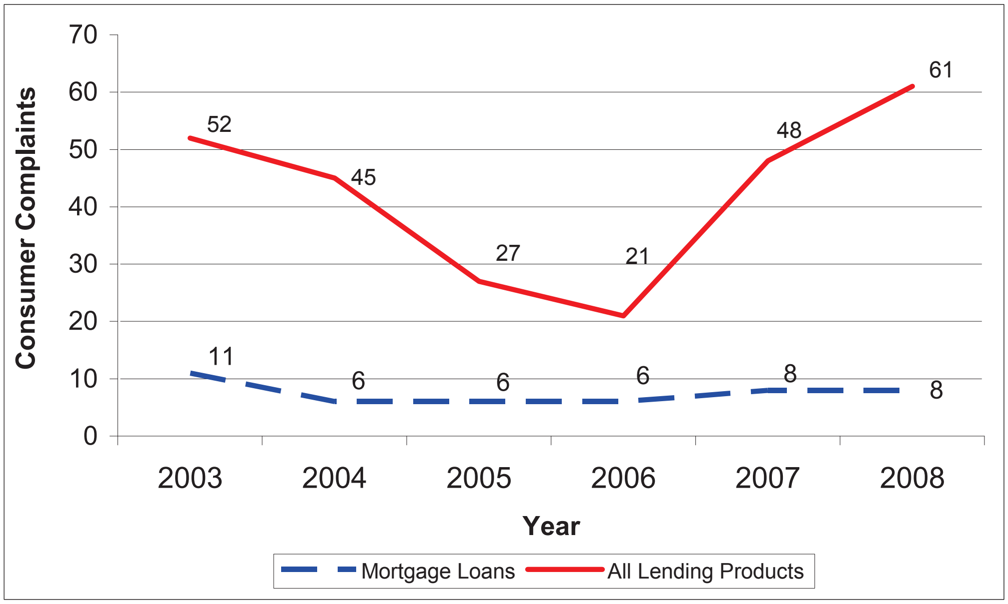
[277] FDIC Response to Interrogatories and Document Requests, Interrogatory Requests 11–12 at pp. 10–12.

[278] FDIC Response to Interrogatories and Document Requests, Interrogatory Request 11 at p. 10.

[279] *Id.*

[280] *Id.* at p. 11. Between 2003 and March 1, 2008, FDIC received 23,519 complaints alleging discrimination in all products/all issues.

Figure 4.6
Consumer Complaints to FDIC, 2003–2008



Source: Federal Deposit Insurance Corporation Response to U.S. Commission on Civil Rights' Interrogatories and Document Requests, Response to Interrogatory Request 12 at p. 11.

Caption: Between 2003 and 2008, FDIC received 254 complaints alleging discrimination in the area of home mortgage loans. More than half of these complaints were filed in 2007 and 2008. During the same period, FDIC received 45 complaints alleging discrimination in all lending products. After declining from 11 to 6 between 2003 and 2004, the number of complaints alleging discrimination in the area of all lending products remained somewhat flat.

In describing its complaint process, the FDIC indicated that, after a complaint is received, it is sent to the bank involved for a response.[281] In its response, the financial institution must address at a minimum: (1) the transaction in question; (2) a description of the financial institution's interaction with the complainant; (3) actions taken by the bank to address their lending policies; and (4) a response to all allegations.[282] The FDIC will decide the course of action it must take based on information the financial institution provides.

If an onsite investigation is needed, the examiner conducting the investigation must prepare a pre-investigation planning memo.[283] During an onsite investigation, interviews are scheduled with the complainant and the financial institution; bank records are reviewed; comparative file analyses are

---

[281] FDIC Response to Interrogatories and Document Requests, Interrogatory Request 12 at p. 12.

[282] *Id.*

[283] *Id.*.

conducted; copies of pertinent documents are obtained; and a complaint investigation report is prepared.[284]

After completion of the onsite investigation, if it is determined that discrimination occurred, the FDIC sends a “15-day letter” informing the banking institution of preliminary findings and giving the institution an opportunity to respond within 15 days.[285]

If the FDIC has reason to believe that a bank has engaged in a pattern or practice of discriminatory conduct, it is statutorily mandated under ECOA to refer the violation to DOJ.[286]

The FDIC indicates that it has referred one complaint relevant to home mortgage lending to DOJ. The complaint alleged discrimination based on race and disability (handicap) because the institution denied a commercial loan application collateralized by the borrower’s residence.[287] The FDIC conducted an onsite investigation, but did not find discrimination based on handicap. However, the FDIC cited the institution for an ECOA violation of discrimination based on race, and found the institution in violation of FHA based on race and familial status.[288] In 2005, the complaint was closed and subsequently referred to DOJ for review, and the banking institution and complainant settled.[289]

7. The Office of the Comptroller of the Currency

OCC, an independent bureau within the United States Department of the Treasury, was created in 1863 under the National Currency Act. OCC now charters, regulates and supervises more than 1,600 national banks as well as 50 federal branches of foreign banks.[290]

OCC examines the activities of banks by conducting on-site reviews and analyzing whether they are operating safely and soundly and in compliance with consumer protection laws and regulations. In addition, OCC approves or denies requests by banks to change their structure and takes supervisory action against banks that do not comply with applicable laws and regulations.[291] In 2008, OCC opened 36,346 consumer complaints involving national banks and logged 58,686 inquiries.[292] Nearly 25 percent of complaints opened in 2008 resulted in monetary compensation.[293] Historically, credit card issues top

---

[284] *Id.* at pp. 12–13.

[285] *Id.* at p. 13.

[286] 15 U.S.C. § 1691e(g) (2006). *See also* FDIC Response to Interrogatories and Document Requests, Interrogatory Request 5 at p. 6.

[287] FDIC Response to Interrogatories and Document Requests, Interrogatory Request 13 at p. 13.

[288] *Id*.

[289] *Id*.

[290] Office of the Comptroller of the Currency, Administrator of the National Banks, *About the OCC*, <http://www.occ.treas.gov/aboutocc.htm> (last accessed Apr. 1, 2009).

[291] *Id.*

[292] Office of the Comptroller of the Currency, Response to U.S. Commission on Civil Rights’ Interrogatories and Document Requests, Response to Interrogatory Request 12 at p. 12.

[293] *Id.*

the list of complaints received by the Customer Assistance Group (CAG), with disputes about checking accounts ranking second, and complaints relating to mortgages ranking third.[294]

Compliance Examinations

OCC's comprehensive fair lending oversight program is designed to: (1) assess and monitor the level of fair lending risk in every national bank; (2) assess compliance with fair lending laws and regulations; (3) obtain corrective action when substantial weaknesses or deficiencies are found in a bank's policies, procedures, and controls relating to fair lending; and (4) ensure that enforcement action is taken when warranted.[295]

To test for and identify potential discriminatory practices, OCC uses a combination of analytical tools, lending information, and risk-based targeted fair lending examinations. OCC's supervisory process entails several steps including: (1) risk assessment and screening; (2) on-site examinations and/or statistical analysis; and (3) enforcement and referrals.[296] Once OCC identifies banks that show signs of heightened fair lending risk, those banks are examined to evaluate whether different outcomes in lending decisions are the result of unlawful discrimination.[297] OCC examiners rely on the *Fair Lending Examination Procedures* handbook, which contains guidance for assessing risks of unlawful behavior involving overt discrimination, underwriting and pricing discrimination, steering, and discriminatory redlining and marketing.[298]

According to OCC, when potentially unlawful discrimination is found, examiners present their findings to bank management for an explanation.[299] If the bank's explanation is inadequate to rebut the preliminary examination findings, the findings are documented and OCC makes a decision as to what supervisory or enforcement action should be taken and on whether a referral to DOJ is required and whether a notification must be provided to HUD of a potential FHA violation.[300] Under its independent enforcement authority, OCC can take a variety of actions against banks and individuals, including cease and desist orders, formal agreements, civil monetary penalties, and the removal and prohibition of "institution-affiliated parties" from participation in the banking industry.[301] OCC was the first federal banking agency to use its cease and desist authority to take a public enforcement action against a bank under ECOA.[302]

---

[294] Office of the Comptroller of the Currency, *Report of the Ombudsman, 2005–2006*, November 2007, p. 22.

[295] Testimony before the U.S. House of Representatives Committee on Oversight and Government Reform, Subcommittee on Domestic Policy, 110th Cong. (Oct. 24, 2007) (Statement of Ann F. Jaedicke, Deputy Comptroller for Compliance Policy, Office of the Comptroller of the Currency), p. 4 (hereinafter cited as Jaedicke Testimony).

[296] *Id.* at p. 5.

[297] *Id.* at p. 7.

[298] *Id.* Office of the Comptroller of the Currency, *Fair Lending Examination Procedures*, April 2006, pp. 22–29, available at <http://www.occ.treas.gov/handbook/fairlep.pdf> (last accessed Aug. 4, 2009).

[299] Jaedicke Testimony at p. 9.

[300] *Id.*

[301] *Id.* at p. 10.

[302] *Id.* at p. 11.

When no violation is found, but there are practices or weaknesses that could expose the bank to unacceptable risk that a fair lending violation could occur, the OCC will instruct bank management to modify its practices or policies to address that risk.[303] According to OCC, its goal is to address fair lending risk before it develops into illegal practices requiring referrals and enforcement actions.[304]

Complaint Processing

As required by the Federal Trade Commission Act, CAG provides guidance and assists consumers in resolving complaints about national banks and their subsidiaries. Attorneys in the Law Department consult closely with CAG in reviewing cases involving allegations of discrimination, predatory lending, or unfair or deceptive practices.

The complaint data CAG collects, summarizes, and makes available to the examiners help them identify practices and activities that merit further review or investigation.[305] When assessing a bank's overall compliance risk and ratings, examiners are required to consider consumer complaint information. Examiners also use complaint data to plan and adjust examinations to better target areas of probable concern.[306]

As reflected in Figure 4.7, complaints alleging predatory lending increased dramatically between 2001 and 2004, from 1 complaint to 32 complaints, respectively. Between 2006 and 2007, the number of complaints alleging predatory lending more than doubled from 32 complaints in 2006 to 79 complaints in 2007. By 2008 the number of complaints alleging predatory lending had spiked to 187, resulting in a 137 percent increase between 2007 and 2008.

The number of complaints alleging mortgage lending discrimination on the basis of race or ethnicity peaked in 1999 at 36. Since 2002, there has been a steady decline in the number of complaints OCC has received alleging mortgage lending discrimination on the basis of race or ethnicity. Between 2002 and 2007, these complaints decreased from 20 to 11 or by 82 percent. In 2008 OCC received 14 such complaints while for the first month of 2009, OCC received 3 complaints. If OCC receives the same number of complaints each month throughout 2009, it is conceivable that the number of complaints will again reach 36.

---

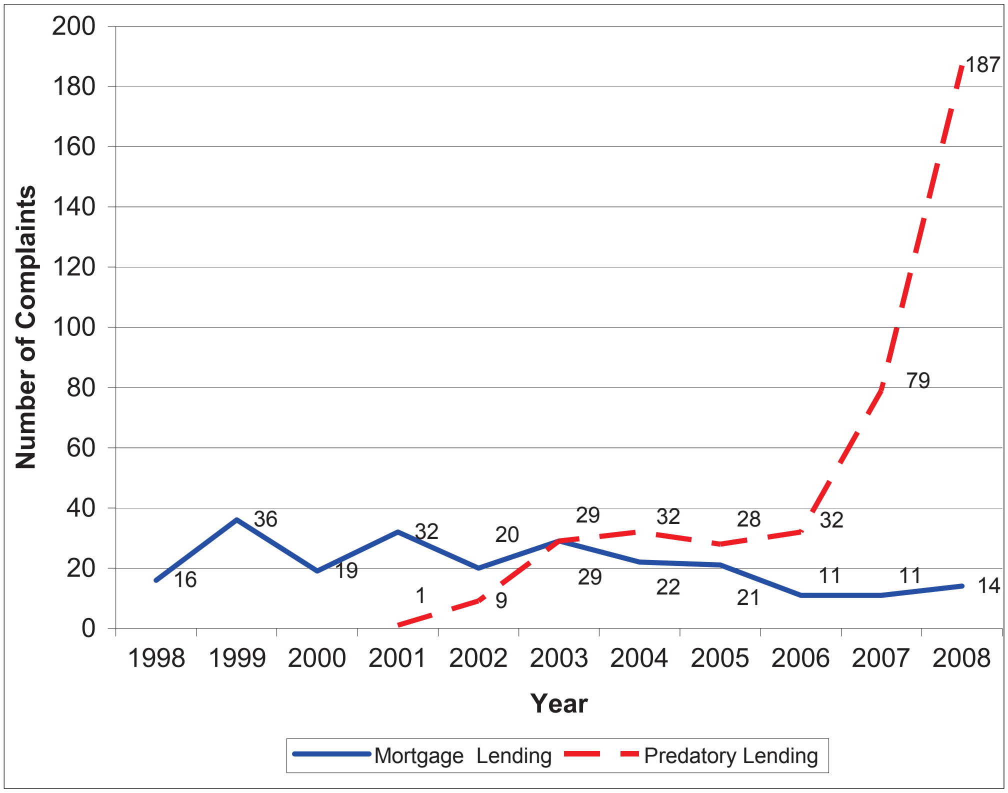
[303] *Id.* at p. 13.

[304] *Id.*

[305] John C. Dugan, Remarks before the Exchequer Club and Women in Housing and Finance (Washington, D.C.), Jan. 17, 2007, p. 13.

[306] *Id.* at p. 16.

Figure 4.7
Mortgage Discrimination (Race/National Origin) and Predatory Lending Complaints Received by OCC, 1998–2008



Source: Office of the Comptroller of the Currency Response to the U. S. Commission on Civil Rights Interrogatories, Response to Interrogatory Request 5 at pp. 7–8. Of the complaints of mortgage lending discrimination on the basis of race or ethnicity received since 1998, 33 were withdrawn. OCC codes a complaint as "withdrawn" when the complainant affirmatively withdraws the complaint, or when the complainant has failed to provide a signed complaint or other requested information needed to process the complaint. If the complainant later provides the information, CAG will reopen the case for processing. Of the remaining cases, 13 were still pending as of February 2009, and the rest have been closed. Cases are closed once the complainant receives the requested resolution, where there is a lack of evidence that the bank's actions conflict with applicable laws, regulations or policies, where the matter is already the subject of private litigation between the complainant and the bank, or where the matter involves a factual dispute.

Caption: In 2003, OCC received 29 complaints alleging mortgage lending discrimination and 29 complaints alleging predatory lending. Between 2004 and 2007, the number of complaints alleging mortgage lending discrimination decreased while the number of complaints alleging predatory lending more than doubled. In 2008, OCC received 187 complaints alleging predatory lending and 14 complaints alleging mortgage lending discrimination.

Referrals to DOJ and/or HUD

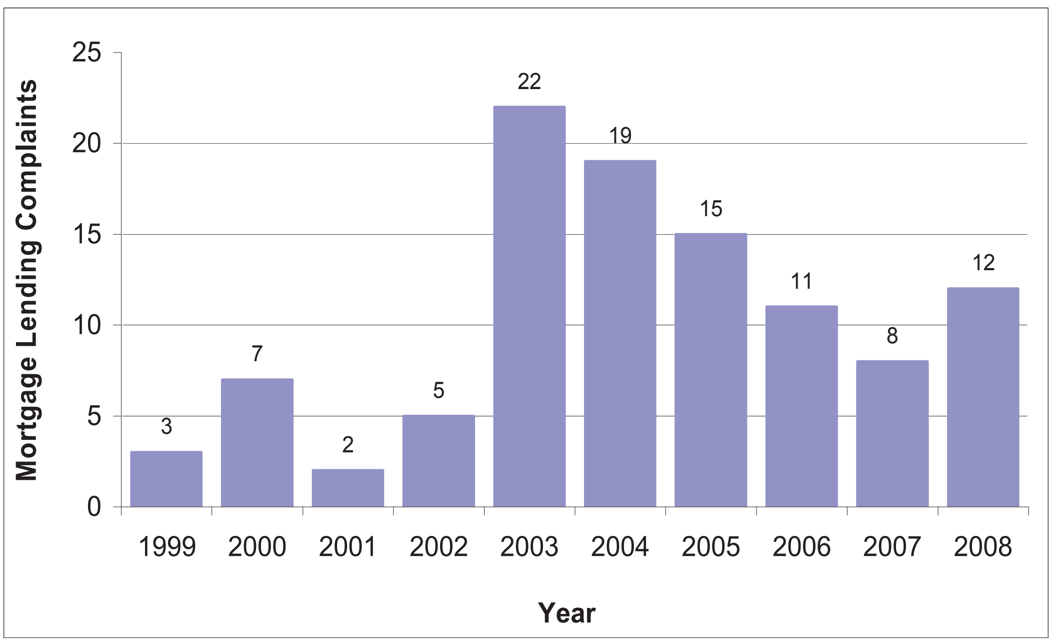
In addition to helping consumers resolve complaints about national banks and their subsidiaries, OCC also refers matters to DOJ or makes notifications to HUD under the referral and notification provisions of ECOA.[307] Between 1999 and 2008, OCC referred 9 matters relating to all types of lending to DOJ.

Between 2003 and 2007 OCC did not make a referral to DOJ, while in 2008 one matter was referred. Between 1994 and 2008 a total of four referrals involving allegations of mortgage discrimination resulted in public consent decrees or settlement agreements. [308]

Referrals to HUD

Under the terms of an MOU with HUD, the OCC forwards complaints of discrimination regarding mortgage lending that it receives involving lenders under its supervisory jurisdiction to HUD. Between 1999 and 2008 OCC forwarded 104 such complaints to HUD.

Figure 4.8
Mortgage Lending Complaints Referred to HUD, 1999–2008



Source: Comptroller of the Currency Response to the U. S. Commission on Civil Rights Interrogatories, Response to Interrogatory Request 13 at p. 13.

Caption: Between 1999 and 2002, OCC referred only a small number of mortgage lending complaints to HUD. The number of referrals to HUD peaked at 22 in 2003 and declined steadily to 8 in 2007. OCC referred 12 complaints to HUD in 2008.

---

[307] OCC Response to Interrogatories and Document Requests, Interrogatory Request 12 at p. 12; Office of the Comptroller of the Currency, *Report of the Ombudsman, 2005-2006*, November 2007, pp. 11–12.

[308] OCC Response to Interrogatories and Document Requests, Interrogatory Request 5 at pp. 5–6.

As shown in Figure 4.8, the number of complaints alleging mortgage lending discrimination which OCC forwarded to HUD peaked at 22 in 2003. Between 2003 and 2007, OCC continuously forwarded to HUD decreasing numbers of complaints alleging mortgage discrimination. During this period, the number of complaints OCC forwarded to HUD declined from 19 to 8, respectively. In 2008, OCC forwarded 12 complaints alleging mortgage lending discrimination to HUD.

8. The Office of Thrift Supervision

OTS, an agency of the United States Department of the Treasury with a traditional and statutory focus on mortgage lending and other forms of consumer lending, serves as the primary regulator of thrifts or savings associations (financial institutions that accept savings deposits and manage mortgage loans). OTS was created in 1989 to secure and regulate savings associations after a period of instability in the 1980s and early 1990s.[309]

Compliance Examinations

OTS compliance oversight examination program is designed to (1) determine the extent and effectiveness of management's efforts toward ensuring adherence to compliance and consumer protection laws and regulations, and (2) determine the extent and effectiveness of management's efforts to maintain a comprehensive and reliable internal compliance program.

OTS examines each savings association every 12 to 18 months to assess the institution's safety and soundness and compliance with consumer protection laws and regulations.[310] Examiners use the Interagency Fair Lending Examination Procedures to determine if there is any unusual fair lending risk and to implement an examination strategy centered on the investigation of those risks.[311]

When OTS has an indication that a lender may have engaged in discriminatory practices, the agency implements supplementary targeted fair lending exams.[312] Such risks can become evident through the screening of HMDA data, the complaint process, and the development of business lines and products that display unusual fair lending risks.[313] In addition, examiners monitor the condition of thrifts through off-site analysis of regularly submitted financial data and regular contact with thrift personnel. OTS examinations and its ongoing supervisory oversight are tailored to the risk profile of each institution.

On a scale of 1 through 5, with 1 being the best rating, as of September 30, 2008, 94 percent of thrifts were rated 2 or better in compliance; two thrifts were rated 4 and two thrifts were rated 5.[314]

---

[309] Office of Thrift Supervision, *Supervising Through the Economic Crisis*, Annual Report – Fiscal Year 2008, pp. 8–9.

[310] Office of Thrift Supervision, Response to U.S. Commission on Civil Rights' Interrogatories and Document Requests, Response to Interrogatory Request 9 at p. 11.

[311] *Id.* at p. 11. The Interagency Fair Lending Examination Procedures are available on the internet at http://files.ots.reas.gov/422220.pdf>.

[312] OTS Response to Interrogatories and Document Requests, Interrogatory Requests 9 & 14 at p. 16.

[313] OTS Response to Interrogatories and Document Requests, Interrogatory Request 9 at p. 11.

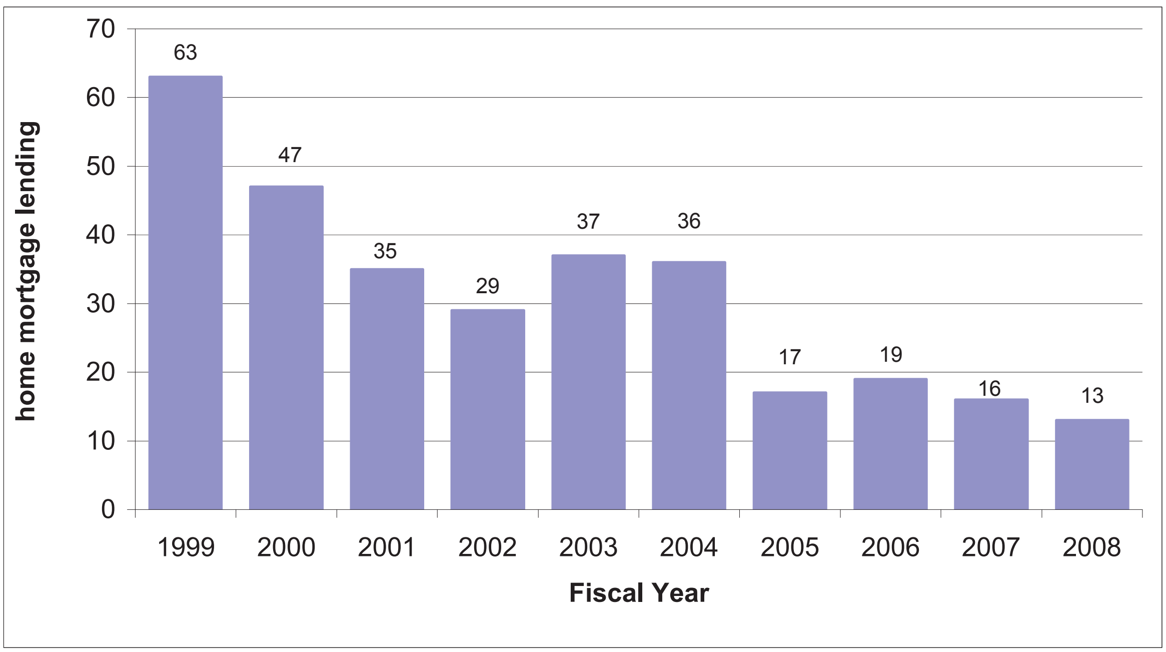
[314] Office of Thrift Supervision, *Supervising Through the Economic Crisis* at p. 25.

Complaint Processing

OTS's Consumer Affairs division handles and processes all consumer complaints and inquiries regarding OTS-supervised institutions.[315] When OTS receives a complaint, the Consumer Affairs division logs it in, reviews it for compliance with federal consumer protection laws and regulations, and provides the consumer the results of the review.[316] If OTS finds a violation of federal consumer protection laws or regulations, the complaint is referred to the appropriate OTS regional supervisory staff for additional action.[317]

As shown in Figure 4.9, from FY 1999 through FY 2008, OTS received 312 complaints alleging home mortgage lending discrimination. Home mortgage lending complaints account for less than 2 percent of the total number of complaints OTS receives during a given fiscal year.[318]

Figure 4.9
Home Mortgage Lending Complaints Received by OTS, 1999–2008



Source: Office of Thrift Supervision Response to the U. S. Commission on Civil Rights Interrogatories, Response to Interrogatory Request 11 at pp. 13–14.

Caption: In 1999, OTS received 63 complaints alleging home mortgage lending discrimination, its largest number since 2008. Between 2000 and 2002, the number of complaints OCC received alleging mortgage lending discrimination decreased from 47 to 29. The number of complaints increased in 2003 and 2004,

---

[315] OTS Response to Interrogatories and Document Requests, Interrogatory Request 12 at p. 15.

[316] *Id.*

[317] *Id.*

[318] OTS Response to Interrogatories and Document Requests, Interrogatory Request 11 at pp. 13–14.

but began decreasing again in 2005. In 2008 OTS received 13 complaints alleging mortgage lending discrimination.

Mortgage lending discrimination complaints were at their highest level in FY 1999. Between FYs 2000 and 2002, complaints alleging mortgage lending discrimination decreased each year, with annual claims going from 47 to 35 to 29. According to OTS data, mortgage lending discrimination complaints increased in FY 2003 and remained level in FY 2004. Figure 4.9 shows that between FYs 2006 and 2008, home mortgage complaints went from 19 to 13, a decrease in claims of 46 percent. For the first quarter of fiscal year 2009, OTS received a total of 1,671 complaints; none alleged home mortgage lending discrimination.[319]

Referrals to DOJ

Pursuant to ECOA, OTS refers matters to DOJ where there is reason to believe that a lender has engaged in a pattern or practice of prohibited discrimination.[320] Such belief can arise through complaints about a lender, screening of HMDA data, or through a compliance examination.[321] With respect to home mortgage lending, OTS referred 7 matters to DOJ between 2004 and 2008,[322] after concluding that there was reason to believe that a pattern or practice of fair lending violations had occurred. OTS has referred two more mortgage related referrals to DOJ in 2009.[323] The violations in these matters were discovered through the examination process as opposed to the complaint resolution process.

---

[319] *Id.* at p. 15.

[320] OTS Response to Interrogatories and Document Requests, Interrogatory Request 12 at p. 15.

[321] *Id.* At its discretion, OTS may also refer matters to DOJ even if that violation does not involve a pattern or practice.

[322] OTS Response to Interrogatories and Document Requests, Interrogatory Request 13 at pp. 15–16.

[323] Office of Thrift Supervision, Response to draft report on *Civil Rights with Respect to the Mortgage Crisis*.

PART III: CREDIT SCORING

CHAPTER 5: CREDIT SCORING AND OTHER FACTORS RELATED TO THE GRANTING AND PRICING OF LOANS

While earlier parts of this report examined laws and policies which seek to prevent discrimination and increase homeownership, this Chapter examines the criteria lenders evaluate both in deciding whether a borrower is sufficiently credit worthy to repay a loan and in establishing appropriate pricing for risk of nonpayment. As discussed below, disparities in the manner and type of credit awarded to various racial and ethnic groups have often been a matter of controversy. Often, disputes have arisen as to whether credit standards accurately reflect creditworthiness.

Most important among the factors lenders review is a widely-used statistical methodology that rates borrowers' credit records, commonly referred to as a credit score. Additional items lenders consider are ratios of the amount of the loan compared to the value of the home the borrower is purchasing and the size of debt relative to the borrower's income. This Chapter examines the accuracy of such criteria in predicting whether borrowers will repay their mortgages, that is, their credit worthiness. It also looks at the underlying racial and ethnic disparities in credit records and other factors that might result in minority groups receiving higher-priced mortgages at a higher rate.

I. Background: The Boston Fed Study

One of the most controversial analyses of disparities in mortgage lending was a 1992 study undertaken by the Federal Reserve Bank of Boston (the Boston Fed).[1]

The purpose in analyzing such disparities was summarized in a contemporary newspaper article discussing the results of the study.

> These statistics don't lie: Black and Hispanic home buyers have a harder time getting mortgages. But why? If lenders discriminate by race, it is up to bank regulators and the Justice Department to enforce anti-bias laws. If, however, minorities are less likely to obtain mortgages mostly because they are more likely to suffer from poverty, the cure — allocating credit by skin color — is arguably worse than the disease… Unequal treatment of minorities isn't necessarily motivated by racism; it can also reflect lesser creditworthiness or other economic disparities.[2]

---

[1] *See* Alicia H. Munnell, Lynn E. Browne, James McEneaney, and Geoffrey M.B. Tootell, *Mortgage Lending in Boston: Interpreting the HMDA Data* (Federal Reserve Bank of Boston, Working Paper No. 92-7, October 1992); Alicia H. Munnell, Geoffrey M.B. Tootell, Lynn E. Browne, and James McEneaney, *Mortgage Lending in Boston: Interpreting HMDA Data*, AM. ECON. REV., vol. 86, no. 1 (March 1996), pp. 25-53 (hereinafter cited as MTBM, 1996). Because there are two somewhat different write-ups with the same title, but only one research study, when it is not necessary to distinguish between the two write-ups, the research will be referred to as the Boston Fed (BF) study.

[2] Peter Passell, *Race, Mortgages and Statistics; The Unending Debate Over a Study of Lending Bias*, NY TIMES, May 10, 1996, at D1, available at <http://www.nytimes.com/1996/05/10/business/race-mortgages-and-statistics-the-unending-debate-over-a-study-of-lending-bias.html> (last accessed July 29, 2009).

In order to address this issue, the Boston Fed report took advantage of the first-time availability of individual loan applicant Home Mortgage Disclosure Act (HMDA) data which included information as to the race of applicants and their success at obtaining a loan. The Boston Fed study also included extensive information from a supplemental questionnaire mailed to 131 financial institutions asking for 38 additional pieces of information on the approximately 3,000 loan applications studied.[3]

The study found that, after controlling for other factors such as financial, employment, and neighborhood characteristics, there still was a "statistically significant" disparity associated with racial discrimination in mortgage lending in the Boston area. Specifically, the study found that the rejection rate for minorities was seven or eight percent higher than for Whites with similar characteristics.[4] As such, the study concluded that discrimination against minorities in mortgage lending continued to be a problem and that federal enforcement of anti-discrimination legislation was inadequate.

Although the report was controversial, receiving both criticism and support,[5] it was cited by the Clinton administration as a justification for aspects of its National Home Ownership Strategy.[6] In addition, its findings prompted the Boston Fed to develop a manual to serve both as a guide to equal opportunity lending as well as a call for stricter enforcement of fair lending laws.[7]

The manual was meant to serve as a "best practice" template for lending institutions and consumer groups. As such, it urged the Board of Directors of lending institutions to "eliminate biases in underwriting standards and practices" to "ensure that they are valid predictors of risk. Special care should be taken to ensure that standards are appropriate to the economic culture of urban, lower-income, and nontraditional consumers."[8] Specifically, the manual urged lenders to reconsider underwriting standards with regard to such considerations as down payments, lack of credit history, increased obligation ratios, employment history, and property appraisals.[9]

---

[3] MTBM, 1996 at p. 28.

[4] *Id.* at p. 33.

[5] *See, e.g*., James H. Carr and Isaac F. Megbolugbe, *The Federal Reserve Bank of Boston Study on Mortgage Lending Revisited*, J. HOUSING RESEARCH, vol. 4, issue 2 (1993), pp. 277-313; Lynne Elaine Browne and Geoffrey M. B. Tootell, *Mortgage Lending In Boston-A Response to the Critics*, NEW ENGLAND ECON. REV., September/October 1995, pp. 53–78; STEPHEN ROSS AND JOHN YINGER, THE COLOR OF CREDIT: MORTGAGE DISCRIMINATION, RESEARCH METHODOLOGY, AND FAIR LENDING ENFORCEMENT (The MIT Press 2002); Theodore E. Day and Stan J. Liebowitz, *Mortgage Lending to Minorities: Where's the Bias*, ECON. INQUIRY, vol. XXXVI (January 1998), pp. 3-28; David K Horne, *Mortgage Lending, Race, and Model Specification*, J. FIN. SERVICES RES., vol. 11, no. 1 (1997), pp. 43-68; David K. Horne, *Evaluating the Role of Race in Mortgage Lending*, FDIC BANKING REV., Spring/Summer 1994, pp. 1-15; Mitchell Stengel and Dennis Glennon, *Evaluating Statistical Models of Mortgage Lending Discrimination: A Bank Specific Analysis*, REAL ESTATE ECON., vol. 27, no. 2 (1999), pp. 299-334.

[6] *See* U.S. Department of Housing and Urban Development, *National Homeownership Strategy: Partners in the American Dream*, May 1995, pp. 6-1, 6-5.

[7] The Federal Reserve Bank of Boston, *Closing the Gap: A Guide to Equal Opportunity* Lending, 1996, available at <http://www.bos.frb.org/commdev/commaff/closingt.pdf> (last accessed July 28, 2009).

[8] *Id.* at p. 13.

[9] *Id.*

The goal of establishing objective measures of creditworthiness is in the interest of both government and lenders. The former needs a benchmark by which to determine whether lending discrimination is occurring. The latter needs to demonstrate its compliance with the same laws. A shared goal, however, does not mean agreement as to what constitutes an objective measure of creditworthiness. This lack of agreement was further exacerbated by the fact that the validity of the Boston Fed data was quickly called into question.

In response to the Boston Fed study, the FDIC dispatched examiners to the 70 FDIC-supervised institutions that participated in the study to investigate their lending patterns. The FDIC examiners undertook "an intensive review" of the loan files that corresponded to rejected applicants. This review turned up a large number of data errors and several systematic reporting errors.[10] The FDIC report concluded that "a detailed examination of individual loan files is likely to be necessary to confirm evidence of lending discrimination" especially because "many loan decisions are influenced by factors that are difficult to capture in a statistical model." [11]

At the same time, the Office of the Comptroller of the Currency (OCC) collected additional data from the OCC's official fair lending examination to compare how models similar to those used by the Boston Fed performed in comparison with the OCC's traditional approach to investigating lending discrimination and to bank-specific models of lending and lending discrimination.[12] This analysis found that a model like the one used in the Boston Fed study carried a likelihood of bias favoring a hypothesis alleging discrimination.[13] In addition, OCC found that the Boston Fed study contained no direct measure of the applicant's capacity to pay the home purchase's closing costs (down payment, taxes, escrows and various fees), despite the fact that the HMDA database itself specifically lists this as a possible reason that mortgage loans could be denied.[14]

Finally, a review undertaken by Theodore E. Day and Stan J. Liebowitz found many data errors in the Boston Fed study, among them:

---

[10] For example, it was learned that the inability of applicants to obtain private mortgage insurance was incorrectly reported as a loan application that was not being accepted for special low-income mortgage programs. It was also found that, while some applicants were rejected for the particular loan terms that they wanted, they were offered alternatives, which the applicants subsequently rejected. However, if they accepted the alternative terms, this was considered an accepted loan application. Horne, *Mortgage Lending, Race, and Model Specification* at p. 48; Horne, *Evaluating the Role of Race* at pp. 5-6. Additionally, the review found that the variable "denial of mortgage insurance" might reflect discrimination on the part of the mortgage insurance company and not the financial institution making the loan. Horne, *Mortgage Lending, Race, and Model Specification* at p. 49; Horne, *Evaluating the Role of Race* at pp. 6-7.

[11] Horne, *Evaluating the Role of Race* at p. 12. As an example of the limitations of this statistical model in measuring discrimination, Horne found that a single lender accounted for 47 percent of all denials to non-Whites in the BF subsample of FDIC supervised institutions. This institution rejected one out of every two minority applicants. However, Horne ascertained that this institution was the sole minority-owned institution in the Boston area. Furthermore, it conducted extensive minority outreach programs, participated actively in a number of affordable housing programs, and 82 percent of all mortgage loans approved by this institution were to non-White applicants.

[12] Stengel and Glennon, *Evaluating Statistical Models*, pp. 299-334.

[13] *Id.* at p. 330.

[14] *Id.* at pp. 307–09, 315–17.

- Many observations for which the imputed interest rates were either too low or too high to be believed.[15]
- Forty-four mortgages classified as rejections were also listed as having been sold on the secondary market.[16]
- At least five mortgage applications where the applicant had a net worth of less than negative one million dollars.[17]
- Out of 1,129 loans with loan-to-value (LTV) ratios of greater than 80 percent, 517 loans, almost half of the total, failed to apply for mortgage insurance yet most of them were approved. Normal practice in the mortgage lending industry is for mortgage insurance to be required with loans with LTV ratios of greater than 80 percent.
- One hundred and fifty-seven applications where the two measures of income, monthly employment income and other monthly income (for both the loan applicant and co-applicant), taken from the Boston Fed researchers extended data and the original HMDA data, are inconsistent by more than 20 percent. Of these, there were 66 instances where the difference was more than 50 percent.

Other reviewers, while acknowledging that the Boston Fed data contained data errors, nonetheless argued that the findings of the study revealed statistical evidence of mortgage discrimination in the Boston metropolitan area.[18]

Partly as a result of the dispute arising from the Boston Fed study, subsequent efforts have been made to attempt to develop improved objective measures of creditworthiness. These methods are the subject of the next section.

II. Methods Lenders Use to Quantify Credit Risk of Prospective Borrowers

One of the primary tools developed to measure creditworthiness is credit scoring, a statistical technology that quantifies credit risk. It ranks individuals, distinguishing those with lower risk of repaying loans from those with higher risks. It uses credit record data, not demographics. Credit scoring formulae generally include five broad types of characteristics—(1) payment history; (2) indebtedness, (3) length of credit history, (4) types of credit used (e.g., credit cards or loans), and (5) the pursuit of new credit—some of which are more important than others.[19]

---

[15] Day and Liebowitz, *Mortgage Lending to Minorities* at p. 22.

[16] *Id.* at p. 23.

[17] *Id.* at p. 24.

[18] *See* Carr and Megbolugbe, *The Federal Reserve Bank of Boston Study on Mortgage Lending Revisited.* Day and Liebowitz claim that even if the errors were corrected, the original findings were rendered statistically insignificant. Day and Liebowitz, *Mortgage Lending to Minorities* at p. 19.

[19] Board of Governors of the Federal Reserve System, *Report to the Congress on Credit Scoring and Its Effects on the Availability and Affordability of Credit*, August 2007, p. 24.

Fair Isaac Corporation developed the widely-used "FICO Scores" that, according to company estimates, are used in more than 75 percent of all mortgage originations. These credit history scores rank consumers by their likelihood of becoming seriously delinquent on any of their credit accounts in the near future (typically over the next 18 to 24 months). FICO scores typically range in value from 300 to 850, with higher scores indicating lower credit risk.[20]

Credit scores, which are calculated from credit history, show a strong relationship to loan default rates for a period following origination. Table 5.1 shows this relationship for loans (not mortgages) where borrowers with FICO scores with high credit worthiness—720 or more—had a default rate of only 1 percent in the first two years after origination. Those with low FICO scores—less than 520—had a default rate of 41 percent during the same timeframe. Indeed, with each reduction in credit worthiness as measured by FICO scores, the default rate increases.

Table 5.1
Default Rate on New Loans for the Two Years (October 2000 to October 2002) after Origination, by FICO Credit Score

FICO score	Default rate
720 or more	1.0%
680-719	4.4%
640-679	8.9%
600-639	15.8%
560-599	22.5%
520-559	28.4%
Less than 520	41.0%

Notes: New accounts were those opened in the six months from October 2000 to April 2001. An account was in default if it had been delinquent for at least ninety days or had any other derogatory credit information within the two years starting in October 2000.

Source: Board of Governors of the Federal Reserve System, Report to the Congress on Credit Scoring and Its Effects on the Availability and Affordability of Credit, August 2007, table 2, p. 133, citing the Fair Isaac Corporation.

Caption: Borrowers with the lowest credit scores, less than 520, have the highest default rate: 41.0 percent. Those with FICO scores of 520 to 559 have a 28.4 percent default rate; those with 560 to 599 have a 22.5 percent rate; those with 600 to 639 have a 15.8 percent rate; those with 640 to 679 have an 8.9 percent rate; those with 680 to 719 have a 4.4 percent rate; and those with credit scores of 720 or more have a 1.0 percent default rate.

[20] Note that Fair Isaac provides statistical models specific to a credit reporting agency based upon that agency's data. Thus, the results of different credit reporting agencies calculating the same individual's FICO score may vary. *Id.* at pp. 22–24.

Note further FICO scores are not the only available credit rating scheme. For example, Vantage Score Solutions LLC developed another formula for credit history scores, known as the VantageScores, which range from 501 to 990. *See Id.* at pp. 24-25.

Lending institutions developed credit scoring to address the need for quick, accurate, inexpensive, and consistent evaluations of credit risk and have come to use the method for broader purposes such as loan pricing (i.e., setting interest rates for each loan according to estimated risk) or estimating loss in the event of default.[21]

On average, interest rates are lower for loans of individuals with higher (i.e., better) credit scores. By way of example, Table 5.2 shows on July 14, 2009, the national average of interest rates for $300,000, thirty-year fixed-rate mortgages for borrowers with FICO scores of 760 to 850 was 4.773 percent. It was 6.362 percent for similar home loans for borrowers with FICO scores ranging 620 to 639. The national average for borrowers with lower credit scores—500 to 619—is unavailable because financial institutions often reject such applications for a thirty-year fixed rate mortgage.[22]

Table 5.2
Average Interest Rate on Fixed-Rate, Thirty-Year Home Loan by FICO Credit Score, July 14, 2009

FICO score	APR
760-850	4.773%
700-759	4.995%
680-699	5.172%
660-679	5.386%
640-659	5.816%
620-639	6.362%

Notes: Rates are national averages on fixed-rate mortgages of $300,000. Elsewhere on a website this source notes that people with credit scores between 500 and 619 are not usually accepted for a 30-year fixed rate mortgage. *See myFICO: Loan Savings Calculator: A Higher FICO Score Saves You Money*, <www.myfico.com/my fico/CreditCentral/LoanRates.asp> (last accessed Mar. 24, 2009).

Source: Informa Research Services, *myFICO: Home Refinance Center: Mortgage rates as of July 14, 2009*, <www.myfico.com/LoanCenter/Refinance/> (last accessed July 14, 2009).

Caption: Borrowers with the highest credit scores receive the lowest interest rates and those with the lowest credit scores receive the highest interest rates. Rates range from 4.773 percent for borrowers with a FICO score of 760 to 850 to 6.362 percent for FICO scores between 620 and 639.

Because of concerns about the use of credit scoring, Section 215 of the Fair and Accurate Credit Transaction Act (Fact Act) directed the Federal Reserve Board and the Federal Trade Commission (FTC) to conduct a study of the effects of credit scoring on the availability and affordability of credit and whether the use of credit scoring affect the availability and affordability of credit to different populations. [23] The resultant study[24] provides much of the data for this section.

---

[21] *Id.* at pp. 29-32.

[22] *See* Table 5.2 and its sources. Figure 5.5, below, representing loans that are reported in the Home Mortgage Disclosure Act database, shows a similar trend in interest rates by credit scores for various racial and ethnic groups.

[23] *See* Fair and Accurate Credit Transactions Act of 2003, Pub. L. No. 108-159 § 215. *See also* Board of Governors of the Federal Reserve System, *Report to the Congress on Credit Scoring and its Effects on the Availability and Affordability of Credit*, August 2007, pp. O-2–O-3, available at <http://www.federalreserve.gov/boarddocs/RptCongress/creditscore/creditscore.pdf > (last accessed July 28, 2009).

The Federal Reserve Board's study, which applied to credit generally, and not mortgage lending specifically, concluded that the use of credit scoring had beneficial effects for *all* borrowers because it improved the availability of credit, its affordability, and the rapidity of loan approval. Furthermore, "[c]redit scoring likely increases the consistency and objectivity of credit evaluation and thus may help diminish the possibility that" "personal characteristics or other factors prohibited by law, including race or ethnicity," influence credit decisions.[25]

A. Effects of Credit Scoring Methods on Minority and Other Populations.

This section examines the possible adverse effects of the use of credit scoring on minorities, as well as its benefits in increasing the amount of lending and decreasing loan processing time. Specifically, it looks at differences in credit records (i.e., credit scoring) as an explanation of racial and ethnic disparities in loans received; and the potential for discrimination in lending when credit scores are the same or equivalent.

1. Racial and Ethnic Disparities in Credit Records

Analysts have developed credit scoring formulae to best measure credit worthiness. Such efforts may not, however, produce equivalent average credit scores for all racial or ethnic subgroups.[26] As one authority explained:

> Credit scoring has not been intentionally discriminatory in its typical uses. Nonetheless, regulators, researchers, and the developers of credit-scoring systems have all recognized that, on average, minorities have lower credit scores than majority populations. Therefore, the use of credit-scoring systems will frequently have an overall discriminatory effect. Such an effect, however, is not illegal if it is based on an overriding business necessity and if there is no less discriminatory way to achieve the underwriting goal. [27]

Indeed, analysts derive credit scores from credit records, and these differ across racial and ethnic groups. Table 5.3 shows racial differences in information contained in credit records. The table indicates that credit records of Whites contain a greater number of loans, leases or bills than those of Blacks. However, twice or even three times as many Blacks have credit records showing signs of payment deficiencies. Specifically, among Blacks, 27.1 percent have a public record of bankruptcy, foreclosure, tax lien, garnishment, or other civil judgment, while only 12.1 percent of Whites have such records. Furthermore, 35.7 percent of Blacks had records of a collection agency involved in obtaining payment for a medical bill and 47.7 had a collection account for other types of bills. In comparison, only 13.7

---

[24] Board of Governors of the Federal Reserve System, *Report to the Congress on Credit Scoring*.

[25] *Id.* at pp. S-3–S-4.

[26] Black and Hispanics, younger individuals, single persons, and residents of lower-income areas or those with higher percentages of minority individuals have lower average credit scores. *Id.* at p. S-4.

[27] The Federal Reserve Bank of San Francisco, *Community Investments Online—Perspectives on Credit Scoring and Fair Mortgage Lending,* Aug. 9, 2007, <http://wwwfrbsf.org/publications/community/investments/0303/article1.html> (last accessed Mar. 25, 2009) (quoting Calvin Bradford, President, Calvin Bradford and Associates, Ltd.) (hereinafter cited as Federal Reserve Bank of San Francisco, *Perspectives on Credit Scoring*).

percent of Whites had collection agencies seeking payment for medical expenses and 13.5 percent for other payments. Finally, 36.0 of Blacks had at least one account with a payment that was 90 or more days delinquent. Only 13.9 percent of Whites had such accounts.

Slightly larger percentages of Hispanics (14.4 percent) have public records of payment deficiencies (such as bankruptcies and foreclosures) than Whites (12.1 percent). However, the percentage of Hispanics with a collection for a medical bill (20.9 %) or an account 90 or more days delinquent (22.7%) are about one and a half times the rates for Whites, and the proportion of Hispanics with a collection for bills other than medical expenses (27.7%) is about double the percent for Whites.

Whites as a group, however, do not have the best credit records. Instead, both Asian Americans/Pacific Islanders and American Indians/Alaskan Natives are less likely to have public records of foreclosures, bankruptcy, liens, collection agency accounts, and delinquent payments than Whites.

Table 5.3
Incidence of Credit Record Item by Demographic Group

Race or Ethnicity	Average number of credit accounts[1]	Percent with a public record of a credit deficiency[2]	Percent with a collection agency account for a medical bill[3]	Percent with any other collection agency account[3]	Percent with any account payment 90 or more days delinquent
Non-Hispanic White	16.7	12.1	13.7	13.5	13.9
Black	13.3	27.1	35.7	47.7	36.0
Hispanic	14.1	14.4	20.9	27.7	22.7
Asian American or Pacific Islander	15.9	8.4	7.1	10.4	12.0
American Indian or Alaskan Native	16.1	12.0	11.0	10.3	12.6
Total Population	**15.4**	**13.1**	**15.7**	**17.5**	**16.3**

[1]A "credit account" refers to each current or past loan, lease, and bill on which creditors and some other entities, such as utility companies and medical facilities, reported detailed information on payment status.

[2]A "public record" is a monetary-related legal record of bankruptcy, foreclosure, tax lien (local, state, or federal), garnishment, or other civil judgment.

[3]A "collection agency account" is a delinquent credit account or unpaid non-credit-related bill that a collection agency is or has handled to obtain payment.

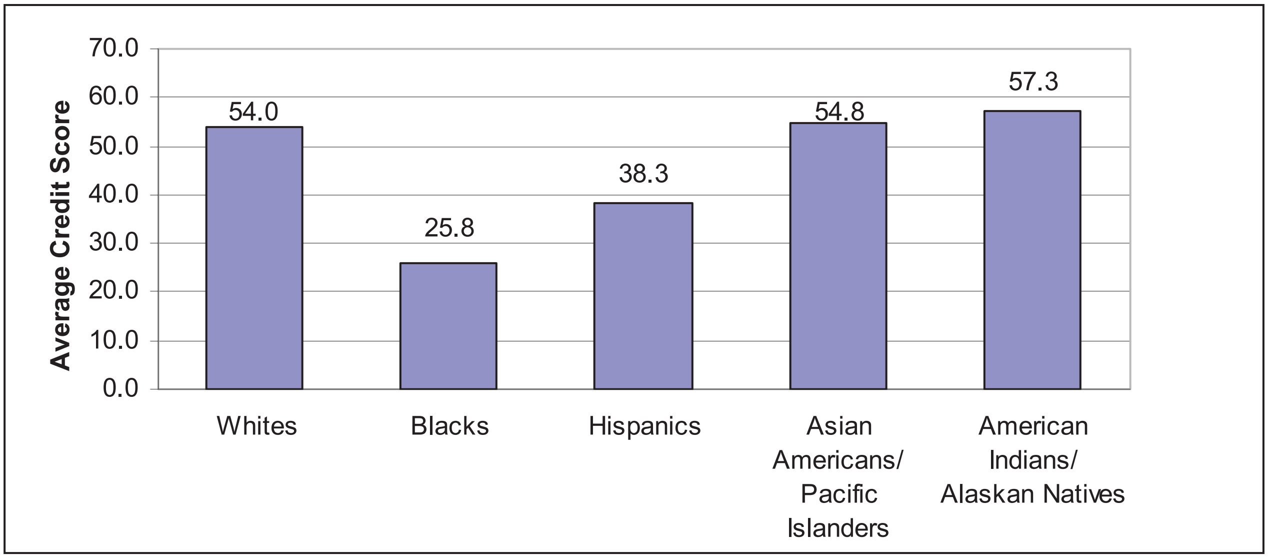
Note: The figures are for the Federal Reserve Board's estimation sample. It included credit records for 200,437 loan applicants. Of these, 133,165 were non-Hispanic Whites; 18,274 were Blacks; 14,702 were Hispanics; 7,906 were Asian American or Pacific Islanders; 366 were American Indians and Alaskan Natives, and 26,024 had unknown race. The Social Security Administration provided information on race or ethnicity, which researchers matched to credit information using social security numbers and date of birth.

Source: Board of Governors of the Federal Reserve System, Report to the Congress on Credit Scoring and Its Effects on the Availability and Affordability of Credit, August 2007, p. 15, 143–44 table 9.

Caption: Looking at racial differences in credit histories, Whites have a higher average number of credit accounts (16.7) than the total population (15.4), while Blacks have fewer (13.3). Blacks have the highest percentage with a public record of credit deficiency (27.1), more than twice as high as Whites (12.1). Blacks also have the highest percentage with a collection agency account for a medical bill (35.7), which is more than the total population (15.7) and Whites (13.7). Blacks and Hispanics have the highest percent with any other collections agency account, 47.7 and 27.7 percent, respectively. The two minorities also have the highest percent with any account payment 30 or more days delinquent: 36 percent for Blacks and 22.7 percent for Hispanics, as compared to 13.9 percent for Whites.

Not surprisingly, given the large differences in the proportions of racial and ethnic groups with records of credit deficiencies, the credit scores calculated on credit records show racial and ethnic disparities. Figure 5.1 shows the average credit scores for racial and ethnic groups.

Figure 5.1
Average Credit Score (on a Scale of 0 to 100) by Racial Group, June 30, 2003



Note: The Federal Reserve Board presents data on different proprietors' credit scores—TransRisk scores and Vantage scores—as well those the researchers derived from their own estimation procedures. The figure presents their own "base" scores.

Source: Board of Governors of the Federal Reserve System, Report to the *Congress on Credit Scoring and Its Effects on the Availability and Affordability of Credit*, August 2007, p. 154 table 14.

Caption: American Indians/Alaskan Natives and Asian Americans/Pacific Islanders have the highest average credit scores, falling at 57.6 and 54.8, respectively, for scores that range from 0 to 100. Blacks are lowest with an average of 25.8. Hispanics' scores, averaging 38.3, fall in the middle between Whites, with 54.0, and Blacks.

Regarding the credit scores shown in Figure 5.1: Because credit scoring models, such as FICO scores (and VantageScores) have different ranges, the Federal Reserve Board's study transformed its estimated credit scores into a scale that ranges from 0 to 100,[28] with a higher score corresponding to greater creditworthiness.

Figure 5.1 shows that on a credit scoring system developed to range between 0 and 100, the average scores for Whites, Asian Americans and Pacific Islanders, and American Indians and Alaskan Natives are 54.0, 54.8, and 57.3, or slightly above the middle of the range. The average scores for Blacks and Hispanics are 25.8 and 38.3, respectively.

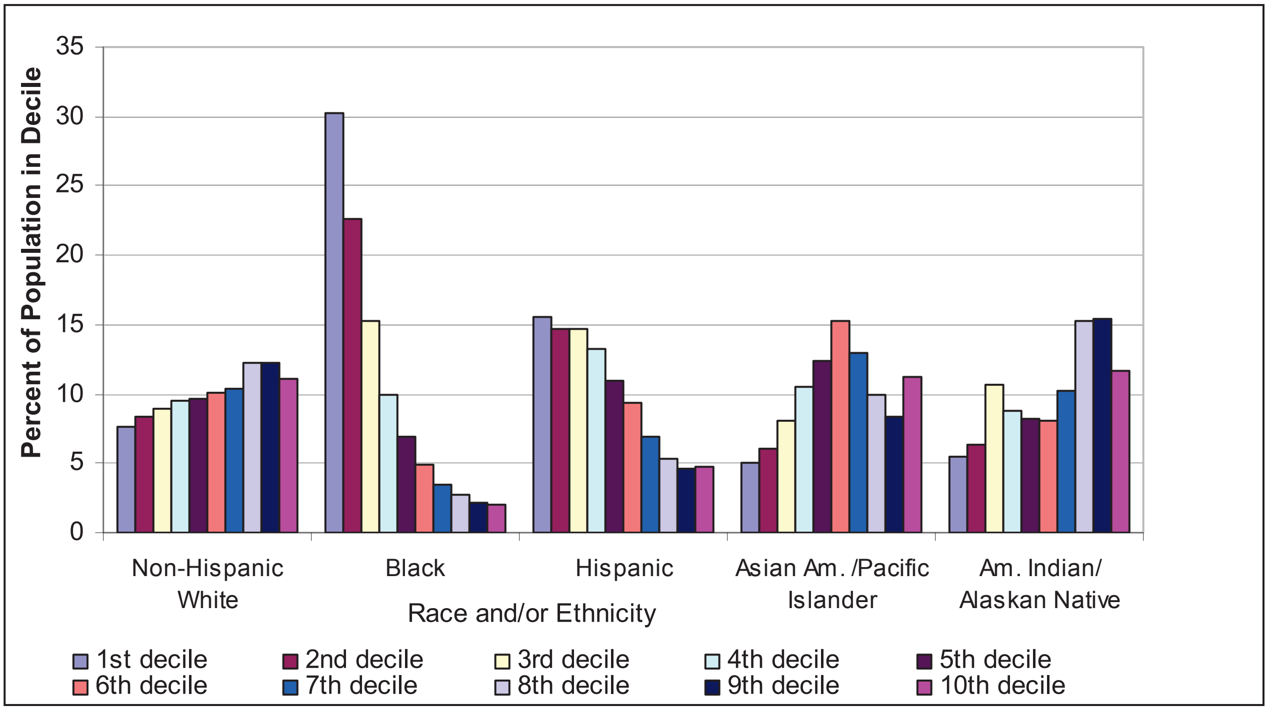
Figure 5.2 reveals the distributions of each racial and ethnic group's credit scores that make up the disparities within each group. The credit scores of Whites are fairly evenly divided throughout the full range of possible scores with slightly larger percentages of them in the 6th through 10th deciles (i.e., having scores of 50 and above) and slightly fewer in the 1st to 5th deciles (with scores below 50). However, Blacks' scores cluster in the lowest range with more than 30 percent in the first decile (a score of 0 to 10 out of 100). Hispanics' scores most often fall in the lower ranges of the credit score distribution but are not as concentrated there as those of Blacks. Asian Americans and Pacific Islanders more often score in the middle of the distribution. American Indians and Native Alaskans may have high or low scores (i.e., 20 to 30) more often than scores in the middle or very low (0 to 20) parts of the range.[29]

---

[28] Board of Governors of the Federal Reserve System, *Report to the Congress on Credit Scoring* at p. 80.

[29] *See id.* at pp. 80–82.

Figure 5.2
Distribution of Credit Scores by Racial Group, June 30, 2003



Note: The credit scores are the Federal Reserve Board's base score, which is normalized to range between 0 and 100.

Source: Board of Governors of the Federal Reserve System, Report to the *Congress on Credit Scoring and Its Effects on the Availability and Affordability of Credit*, August 2007, p. 6 table 14.

Caption: The distribution of credit scores for Blacks is highly skewed to the lower end, with 30 percent falling in the first decile (the lowest credit scores) and around 23 percent falling in the second decile. Hispanics are also skewed to the left, with around 15 percent in each of the first three deciles. The non-Hispanic White population is fairly evenly distributed among deciles, with only slightly more than 10 percent falling in the eighth and ninth percentiles. Both the Asian American/Pacific Islander and American Indian/Alaskan Native populations have credit scores that are more heavily distributed in the higher deciles (i.e., more credit worthy).

Differences in credit scores across groups were partly reduced when the researchers considered other location and demographic characteristics, such as income. However, significant differences remained.[30] For example, the differences in Black and White average credit scores shown in Figure 5.1 (i.e., the White average of 54.0 minus the Black average of 25.8) is 28.2 points on a scale of 0 to 100. When researchers took account of the fact that Blacks and Whites differ in income, age, gender, marital status, and certain neighborhood characteristics, the disparity between Blacks and Whites was reduced by 13.4 points on this scale. Yet the reduction is less than half of the overall difference.[31] For Hispanics, ethnic

[30] *Id.*

[31] *Id.*

differences on these demographic factors reduce the disparity from Whites of 15.7 to 3.9.[32] Thus, only about a quarter of the overall disparity remained for Hispanics.

2. How Well Do Credit Records Predict Loan Performance For Racial and Ethnic Groups?

Scores based on credit history predict credit risk for the population as a whole. The Federal Reserve study shows that over any credit-score range, the higher (better) the credit score, the lower the observed incidence of default. *See* Table 5.1.

The Federal Reserve study indicated that scores based on credit history predict credit risk for all major demographic groups. In other words, for every race or ethnic group, the higher (better) the credit score, the lower the observed incidence of default. The report states "credit scores consistently predict *relative* loan performance within all population groups; that is, for all populations, the percentage of individuals experiencing a serious delinquency on one or more of their credit accounts consistently declines as credit scores increase.[33] *See* Figure 5.3.

In some cases, the Federal Reserve study found differences across groups in average performance for individuals *with the same score.* In particular, Blacks and persons living in lower-income or minority neighborhoods *underperform,* that is, given their credit score their default rate exceeds the rate of other races or neighborhoods. In contrast, Asian Americans, foreign born individuals (particularly recent immigrants), and those living in higher-income areas over perform (i.e., default less often). [34] *See* Figure 5.3, noting that the line for Blacks is higher, meaning greater frequency of "bad" performance, throughout the range of credit scores. The Federal Reserve Board found that analyses with other factors did not substantially explain these racial and neighborhood differences.[35]

As a banking counsel explained, banks' use of validated credit-scoring systems "reduces the subjectivity of the final credit decision," ensures "standard treatment of applicants" and "allows compliance officers to better monitor fair-lending compliance." Describing a recent legal matter, he indicated that fair-lending violations arose, not as a result of the credit-scoring model, but from ignoring it as a factor in the lending decision.[36]

---

[32] *Id.*

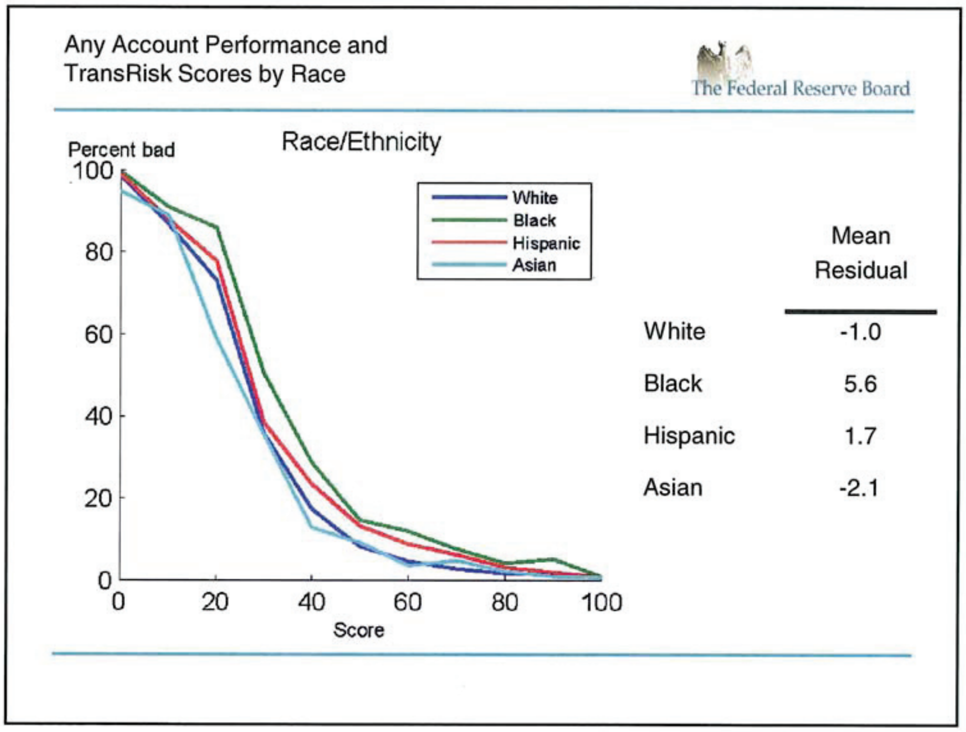
[33] *Id.* at p. S-4.

[34] *Id.* at pp. S-4–S-5.

[35] *Id.*

[36] Federal Reserve Bank of San Francisco, *Perspectives on Credit Scoring* (quoting Paul Smith, senior counsel of the American Bankers Association).

Figure 5.3
Bad Performance on Any Account by Credit Score and Racial Group

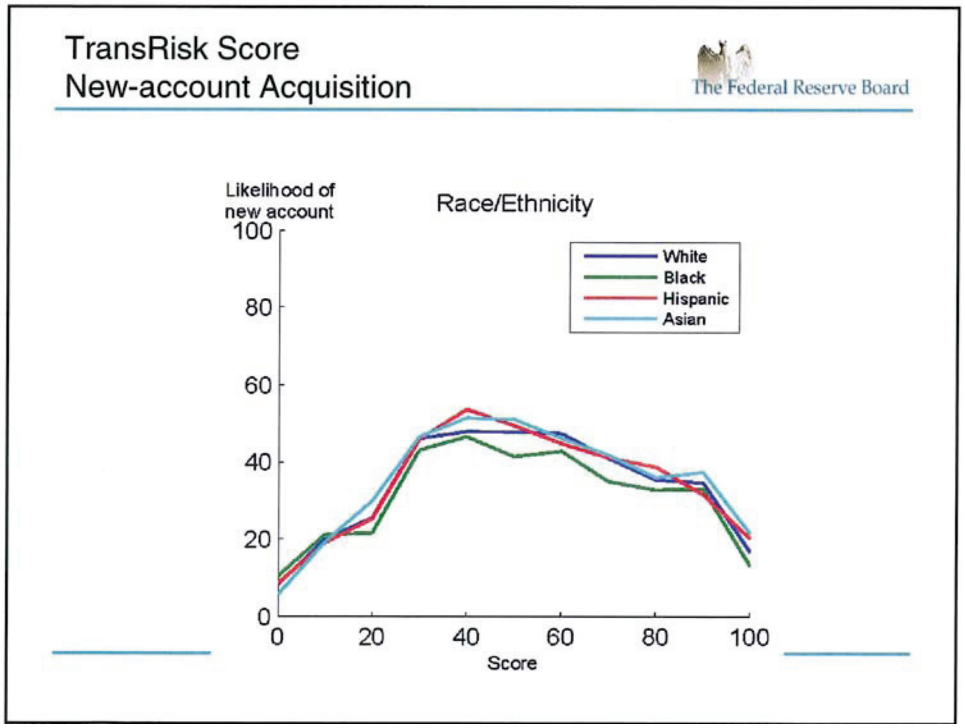


Source: The Federal Reserve Board, "Credit Scoring and Access to Credit," Briefing by staff of the Board of Governors of the Federal Reserve System for staff of the U.S. Commission on Civil Rights, Jan. 7, 2009, p. 9. *See also* Board of Governors of the Federal Reserve System, *Report to the Congress on Credit Scoring and Its Effects on the Availability and Affordability of Credit*, August 2007, p. 244 figure 6.A.

Caption: For all racial/ethnic groups, the percent bad performance on any account decreases as credit scores increase.

Figure 5.4 reflects differences between the various groups, even when they have the same or similar credit scores. Overall, Figure 5.4 indicates that the likelihood of getting a new loan, although never above about 60 percent, varies according to credit score. It is lowest—about 10 percent—for those with low credit scores, but also low—about 20 percent—for those with the highest credit scores. It is highest for those with credit scores of about 40 on a normalized scale ranging between 0 and 100. The probability of receiving a new loan is slightly lower for Blacks than other groups for credit scores throughout most of the range. For individuals with credit scores of about 40 on this scale, Asian Americans and Hispanics are more likely to get new loans than Whites.

Figure 5.4
Probability of Getting a New Loan by Credit Score and Racial Group



Source: The Federal Reserve Board, "Credit Scoring and Access to Credit," Briefing by staff of the Board of Governors of the Federal Reserve System for staff of the U.S. Commission on Civil Rights, Jan. 7, 2009, p. 11. *See also* Board of Governors of the Federal Reserve System, *Report to the Congress on Credit Scoring and Its Effects on the Availability and Affordability of Credit*, August 2007, p. 254 figure 8.

Caption: For all racial/ethnic groups, the probability of getting a new account increases from near 0 or 10 percent for the lowest credit scores to 40 to 50 for scores of about 40 (on a scale of 0 to 100), and declines to slightly for scores ranging as high as 80 or 90.

3. What Adverse Effects Does the Use of Credit Scores Have on Racial and Ethnic Groups?

a. Discrimination in Credit Histories May Contaminate Credit Scores

Subjectivity and potential discrimination enter into the data of credit reporting agencies because, for example, creditors serving higher-risk customers are more aggressive in reporting late payments.[37] Indeed, business advisors recommend developing a collection strategy that focuses recovery efforts on the highest-risk accounts. This strategy may identify the highest-risk accounts using customers' demographics and past payment behavior. It may then establish procedures to initiate recovery efforts for risky accounts among those that are only recently delinquent, but delay such actions for more credit

[37] Scott Susin, Economist, Office of Systemic Investigations, FHEO, Failures of Credit Scoring, slide presentation, HUD FHEO Policy Conference, Apr. 9, 2008, pp. 12–13 (hereinafter cited as Susin, Failures of Credit Scoring).

worthy accounts. Thus, businesses may reduce recovery costs by identifying accounts which will warrant little or no resources to resolve.[38]

b. The Lack of Credit Scores

Researchers estimate that 35 to 54 million adults lack credit scores because they have no credit files at all or have "thin files," meaning those with insufficient information to calculate a standard credit score. Because creditors have difficulty predicting performance for consumers with little or no credit history, they are reluctant to extend credit.[39]

As reflected in Table 5.4, members of minority groups are more likely than Whites or Asian Americans to have no credit record on which to base credit scores.

Table 5.4
Percent of Racial and Ethnic Groups With No Credit History on Which to Base Credit Scores

Race or Ethnicity	Percent
Non-Hispanic White	8.8%
Black	17.6%
Hispanic	12.8%
Asian American	8.8%
American Indian	7.3%
Total	10.2%

Note: Percentages are calculated excluding a category of "Unknown Race." Note that another author has reported the same information with different results based on the author's estimates correcting for the presence of those with unknown race. *See* Scott Susin, Economist, Office of Systemic Investigations, FHEO, Failures of Credit Scoring, slide presentation, HUD FHEO Policy Conference, Apr. 9, 2008, p. 10.

Source: Compiled by U.S. Commission on Civil Rights from Board of Governors of the Federal Reserve System, *Report to the Congress on Credit Scoring and Its Effects on the Availability and Affordability of Credit*, August 2007, p. 142 table 9.

Caption: Sources indicate that 17.6 percent of Blacks had no credit history on which to base credit scores. Only 12.8 percent of Hispanics were in this situation, compared to 8.8 percent of non-Hispanic Whites, and Asian Americans, and 7.3 percent of American Indians. Just over 10 percent of the total population lacks a credit history.

Because of concerns that Americans new to the credit market may be missing out on the benefits of the credit reporting system, in 2004, the Federal Trade Commission studied whether any common financial

---

[38] *Id.* at pp. 14-18.

[39] Michael A. Turner and Amita Agarwal, *Using Non-Traditional Data for Underwriting Loans to Thin-File Borrowers: Evidence, Tips and Precautions*, J. RISK MGMT. FIN. INSTITUTIONS, vol. 1, no. 2 *(*2008), p. 166 & p. 179 n.2 (hereinafter cited as Turner and Agarwal, *Underwriting Loans*). Other industry experts rely on this article's estimates. *See ,e.g.,* Susin, Failures of Credit Scoring at p. 1.

Note that a 2003 survey found that "no credit score" was the most important reason why mortgage lenders did not submit loan applications to an automated underwriting system through which borrowers benefited by providing less documentation than traditional underwriting procedures, paying lower origination fees, and obtaining quicker lending decisions. Federal Trade Commission, *Report to Congress Under Sections 318 and 319 of the Fair and Accurate Credit Transactions Act of 2003,* p. 78 (December 2004) (hereinafter cited as FTC 2004 Report to Congress).

transactions that are not generally reported to the bureaus could be useful in evaluating creditworthiness. The FTC's report concluded that regular bill payments, particularly for rent and utilities, were useful for establishing credit. However, barriers arise in the means of reporting these payments to credit bureaus. The diffuse housing market and the lack of centralized data collection impair the reporting of rental payments. Similarly, barriers such as cost, the terms of the Fair Credit Reporting Act,[40] some state privacy laws, and possible disincentives arising from state regulatory systems, make it often impracticable to report utility payments.[41]

One study suggests that mainstream lenders generally assume that applicants with little or no information are high-risk or reject them because of the lack of information. Yet, research based on the inclusion of utility payments indicates that consumers who were unscoreable using traditional methods, were not clustered in the bottom rung of credit scores, but rather fairly evenly distributed throughout the range of scores. Including utility payment information also improves the risk sorting (i.e., the accuracy of credit scores) among individuals who were scoreable without utility data.[42]

Credit score vendors are experimenting with developing nontraditional credit scores. Such scores rely on payment records for rent, utility, telecommunications, and other bills that are not reported to credit bureaus except when payments are late or in default.[43]

For example, one national consumer reporting agency and credit bureau, known as "Payment Reporting Builds Credit" or PRBC, collects, stores, scores, and reports bill payment data to enable consumers and small businesses to build a credit file to demonstrate creditworthiness. Consumers can either order a verification of past payments or register to build (i.e., voluntarily report through a third party) their record of future payments. In 2009, PRBC would verify rental history for $20 or rental history and 3 additional payment accounts, such as electricity, phone, and cable, for $65. For building a credit history, consumers enroll themselves and pay a monthly fee (about five dollars) to an on-line bill payment service that automatically reports information to PRBC. With the consumer's consent, PRBC then sells credit reports to lenders showing on-time bill payment for up to the past three years.[44]

---

[40] 15 U.S.C. § 1681 et seq. (2006).

[41] FTC 2004 Report to Congress at pp. vii, 78-85. For example, enhanced privacy protections in California, New Jersey, Ohio, and Texas prohibit the onward transfer of data on customers' utility and telecommunications payments. Furthermore, in 2008, other states had newly introduced legislation on consumer credit reporting to impede the ability of utility companies to report to credit reporting agencies. Turner and Agarwal, *Underwriting Loans* at p. 178.

[42] Turner and Agarwal, *Underwriting Loans* at pp. 166, 171-72. Other industry experts rely on this article's estimates. *See, e.g.,* Susin, Failures of Credit Scoring at p. 1.

Note that a 2003 survey found that "no credit score" was the most important reason why mortgage lenders did not submit loan applications to an automated underwriting system through which borrowers benefited by providing less documentation than traditional underwriting procedures, paying lower origination fees, and obtaining quicker lending decisions. FTC 2004 Report to Congress at p. 78.

[43] Susin, Failures of Credit Scoring at p. 7.

[44] *See* Credit Plus, Inc., *PRBC—Non-Traditional Credit Information and Score,* 2007, <http://www.creditplus.com/prbc.html> (last accessed Mar. 25, 2009); Payment Reporting Builds Credit (PRBC), *PRBC Frequently Asked Questions—FAC,* 2009, <http://ez.prbc.com/main/faq.php?passpath=main/faq.php&> (last accessed Mar.

Acceptance of nontraditional credit scores has been slow. For example, Fannie Mae, Freddie Mac, and big lenders have not yet incorporated them into automated underwriting systems.[45] Even proponents of using nontraditional data advise lenders to proceed with caution, despite the promising results of early tests of utility and telecommunications payment data. They urge that lenders test the value of such data in specific contexts, using such data to supplement, not replace, traditional methods.[46]

III. Factors Other than Credit Score that Relate to Differences in Lending for Minorities and Whites

Apart from the borrower's credit scores, financial institutions often consider other factors in making loans that could account for differences in the frequency with which minority group members receive subprime loans, or higher interest rates. Because additional factors may capture credit worthiness that is not represented in credit scoring models, disparities may arise even when Whites and members of other racial/ethnic groups have the same credit score.[47]

As other factors are considered, however, it becomes more difficult to draw consistent conclusions as to whether lending decisions are based on factors other than creditworthiness. For example, various studies undertaken to review whether disparities are based on possible discrimination have varied as to the factors reviewed, the time period examined, the sample size considered, and the type of data reviewed.[48]

By way of example, in analyzing racial and ethnic differences in interest rates of mortgages, one very recent study by the Federal Reserve Bank of New York found that differences in risk accounted for the significantly higher interest rates Black borrowers received. The study measured the risk of mortgages not only with credit scores, but also with loan-to-value and debt-to-income ratios, the level of documentation used in the underwriting, the loan amount, and the type of property used as collateral.[49] It also found that the neighborhood of the mortgaged home mattered. Considering all of the listed factors, the study found the following:

25, 2009); Payment Reporting Builds Credit (PRBC), *Build Credit With Every Bill You Pay,* 2009, <http://ez.prbc.com/consumers/how/futurepay.php> (last accessed Mar. 25, 2009).

[45] Susin, Failures of Credit Scoring at p. 8.

[46] Turner and Agarwal, *Underwriting Loans* at pp. 177-78.

[47] Overall wealth and creditworthiness are not necessarily completely captured by credit scores. In his regard, a recent study indicated that: "Regardless of age and income, African-American and Hispanic workers are less likely to participate in their company 401(k) plans, and when they do contribute, they save at much lower rates than whites." *See* Ariel/Hewitt Study, *401(k) Plans in Living Color: A Study of 401(k) Savings Disparities Across Racial and Ethnic Groups* (2009).

[48] *See, e.g.,* Andrew Haughwout, Christopher Mayer, and Joseph Tracy, Federal Reserve Bank of New York, *Subprime Mortgage Pricing: The Impact of Race, Ethnicity, and Gender on the Cost of Borrowing,* staff report no. 368, April 2009, p. 2.

[49] *See id.* at pp. 13, 15, 19–20, 27–28 table 3.

> Our results provide no evidence of adverse pricing by race, ethnicity or sex of the borrower in either the initial rate or the reset margin. If any pricing differential exists, minority borrowers appear to pay slightly lower rates. We also find that borrowers in Zip Codes with a higher percentage of black or Hispanic residents or a higher unemployment rate actually pay slightly lower mortgage rates. [50]

In making their finding, the authors of said study were careful to describe the parameters of their research. In this case the study involved a sample of more than 75,000 adjustable-rate mortgages for the month of August 2005 using a new dataset created by "merging information on the race, ethnicity, and gender of mortgage borrowers as reported under HMDA with mortgage pricing and risk variables reported by LoanPerformance (LP)."[51] As noted by the authors, the merged dataset allowed them "to examine racial, ethnic, and gender differences in mortgage lending, controlling for both the risk profile of the mortgage and the characteristics of the neighborhood where the property is located."[52]

In a similar fashion, a 2007 study used many of the same factors to examine racial and ethnic differences with regard to both the probability of obtaining a subprime loan and the pricing of mortgages. This study involved a review of data including "APR, typical underwriting variables such as loan-to-value ratios (LTV), debt-to-income ratios (DTI), and FICO scores, as well as other variables that likely affect mortgage pricing, such as documentation status, the existence of prepayment penalties, and sourcing channel."[53] The dataset for this study included over one million loan-level records of originations for the years 2004 and 2005 from over 20 lenders and/or their subsidiaries.

Taking all such factors into consideration, the study noted that, although minority borrowers pay higher APRs than non-minority borrowers, "the vast majority of APR differentials between minority and non-minority mortgage borrowers can be explained by observable characteristics appropriately associated with underwriting and pricing outcomes."[54]

By way of contrast, a 2006 study undertaken by the Center for Responsible Lending came to a different conclusion. This study used 2004 HMDA data merged with a propriety dataset which resulted in a sample of about 177,000 subprime loans. The analysis included all of the HMDA variables, as well as such credit-related variables as FICO scores, LTVs, documentation status, and term to maturity. Using this dataset, the report found: "Our findings show that, for most types of subprime home loans, African-American and Latino borrowers are at greater risk of receiving higher-rate loans than white borrowers, even after controlling for legitimate risk factors. [55]

---

[50] *Id.* at p. 21.

[51] *Id.*

[52] *Id.* at p. 2.

[53] Marsha J. Courchane, *The Pricing of Home Mortgage Loans to Minority Borrowers: How Much of the APR Differential Can We Explain?*, J. REAL ESTATE RES., vol. 29, no. 4 (2007), p. 429.

[54] *Id.* at p. 431.

[55] DEBBIE GRUENSTEIN BOCIAN, KEITH S. ERNST AND WEI LI, CTR. FOR RESPONSIBLE LENDING, UNFAIR LENDING: THE EFFECT OF RACE AND ETHNICITY ON THE PRICE OF SUBPRIME MORTGAGES 3 (May 2006).

As the dispute surrounding the Boston Fed study indicated, studies relating to disparities in mortgage lending are likely to remain controversial. Absent consensus on the factors to be examined and the variables to be considered, there will always be a basis for objection or dissent.

Clearly, however, there has been an attempt on the part of the lending industry to develop objective measures of creditworthiness. As additional studies are undertaken, continued attempts should be made to determine if existing disparities between races and ethnicities are the result of current discrimination or of other factors relating to creditworthiness. The adoption of policies based on false premises will not benefit either borrowers or lenders.

As noted by the Federal Reserve Bank of New York in its April 2009 study:

> [T]hese results suggest the possibility that subprime lending did serve as a positive supply shock for credit in locations with higher unemployment rates and minority residents. These results are consistent with economies of scale and subprime lending. We believe that further research is needed to understand better how this additional credit impacted these locations. Policy responses today often consider how to limit subprime lending in the future, but it is important to understand any positives that may also have occurred along with the down sides of subprime lending.

METHODOLOGY USED IN REPORT

METHODOLOGY USED IN REPORT

In compiling the tables and figures of this report, the Commission drew data from various sources. Where possible the Commission relied on publicly available, national data and federal agency reports. The Commission sought additional information through interrogatories issued to federal agencies, particularly regulatory enforcement agencies and government-sponsored enterprises. It further supplemented this information with the statements of experts who participated in a Commission sponsored briefing held March 20, 2009. Finally, staff examined research efforts of financial industry experts, academicians, and policy analysts. Key sources are listed below along with brief discussions of their limitations and variations in their definitions of key factors such as race.

Bureau of Census Data

The Commission used the Bureau of the Census' American Housing Survey,[1] Decennial Census of Housing,[2] Current Population Survey/Housing Vacancy Survey[3] and the American Community Survey[4] to obtain data on homeownership rates. In its surveys, the concept of race as used by the Bureau of the Census reflects self-identification according to the race or races with which survey participants most closely identify. The race categories include both racial and national-origin groups. The racial categories used in the 1990 census data products adhere to the guidelines in the Federal Statistical Directive No. 15, issued by the Office of Management and Budget (OMB). These racial categories were: (1) White, (2) Black, (3) American Indian, (4) Eskimo, or Aleut, (5) American Indian, (6) American Indian Tribe, (7) Eskimo, (8) Aleut, (9) Asian or Pacific Islander, (10) Asian, and (11) Pacific Islander, and (12) Other Race. Revisions to OMB Statistical Directive 15 designated five races: (1) White, (2) Black or African American, (3) American Indian and Alaska Native, (4) Asian, and (5) Native Hawaiian or other Pacific Islander and two ethnic origin categories (Hispanic or Latino and non-Hispanic or Latino). The American Housing Survey adopted the new terminology in 2003. Race and Hispanic origin are two separate and distinct concepts and people who are Hispanic may be of any race. This overlap is the main comparability issue when users want to compare a specific race with the number of Hispanics, or even when comparing the population size of one race group with another. The Commission used the racial categories as revised by OMB.

[1] The U.S. Census Bureau, American Housing Survey <http://www.2010census.biz/hhes/www/housing/ahs/ahs.html>.

[2] The U.S. Census Bureau, Census of Housing <http://www.census.gov/hhes/www/housing/census/histcensushsg.html>.

[3] The U.S. Census Bureau, Housing Vacancies and Homeownership <http://www.census.gov/hhes/www/housing/census/histcensushsg.html>.

[4] The U.S. Census Bureau, American Community Survey <http://www.census.gov/acs/www/index.html>.

The Home Mortgage Disclosure Act Data

The Commission obtained Home Mortgage Disclosure Act (HMDA) data for 1999 to 2007 from database tables posted on the Federal Financial Institutions Examination Council's (FFIEC) website.[5] HMDA requires certain lending institutions to collect, disclose, and report data on the personal characteristics of mortgage borrowers and loan applicants, the type of loan, and certain financial data. HMDA's many purposes include helping the public determine if lending institutions are meeting the housing credit needs of their communities, providing the public with loan data that can assist in identifying potential risks for patterns of discrimination, and aiding federal agencies in enforcing antidiscrimination laws.[6] In 2002, the Federal Reserve increased the reporting requirements for covered institutions, requiring them to incorporate into HMDA reporting the revised standards for collecting race and ethnicity information as required by OMB and to collect mortgage loan pricing data with an annual percentage rate of 3 or more percentage points higher than the yield for a comparable term Department of the Treasury security. These types of loans are referred to as "higher price." Only "higher price loans" are reported and as a result the price of loans below that threshold is unknown. Institutions did not begin reporting pricing data until 2005. Transactions occurring in the current year are not reported until the following year. The Commission presented pricing data for 2004 to 2007.

When analyzing and presenting tabular and graphic data extracted from the HMDA database tables, the Commission classified individuals into the following racial and/or ethnicity groups throughout this report: (1) White, (2) Black, (3) American Indian, (4) Asian, (5) Native Hawaiian, and (6) Hispanic. Borrowers who fall into the "2 or more minority races," "joint (white/minority race)," or "race not available" categories are excluded.

The National Mortgage Bankers Association Data

The National Mortgage Bankers Association provided the National Delinquency Survey Data used in this report. For 1998 to 2008, the Commission used the National Delinquency Survey data for both tabular and graphic information on 30-, 60-, and 90-day delinquency rates and foreclosure rates for adjustable and fixed rate conventional and FHA prime and subprime loans. The Commission also presented this survey's information on veterans' (VA) loans.

---

[5] Federal Financial Institutions Examination Council, <http://www.ffiec.gov/hmdaadwebreport/NatAggWelcome.aspx>.

[6] U.S. General Accountability Office, *Fair Lending: Data Limitations and the Fragmented U.S. Financial Regulatory Structure Challenge Federal Oversight and Enforcement Efforts*, Washington, DC, July 2009, p. 11.

Information From Federal Agencies

For this report the Commission cited numerous federal agency documents, including annual or periodic performance reports, oversight reports, and information routinely provided to the public. Such documents include, for example, the Department of Housing and Human Services' Federal Register Notices on goals; Fannie Mae and Freddie Mac's performance against HUD housing goals; the Office of Federal Housing Enterprise Oversight's annual reports on mortgage markets and the enterprises, the Department of Justice's annual reports on the enforcement of ECOA, and the Federal Bureau of Investigation's reports on fraud. In addition to using such reports, many of which are available on agencies' websites, the Commission visited staff at 11 agencies and sought information through responses to interrogatories. The agencies were the Department of Housing and Urban Development, the Department of Justice, the Federal Trade Commission, the Federal Housing Finance Agency, Freddie Mac, Fannie Mae, and the five regulatory agencies which comprise the Federal Financial Institutions Examination Council: the Federal Reserve, the National Credit Union Administration, the Federal Deposit Insurance Corporation, the Office of Thrift Supervision, and the Office of the Comptroller of the Currency.

Experts' Briefing of the Commissioners

On March 20, 2009, the Commission held a briefing at which experts were invited to make presentations and engage in discussion on whether policies intended to prevent discrimination in housing and mortgage lending contributed to the mortgage crisis and whether lenders' policies unfairly targeted or otherwise discriminated against minority homeowners. The panelists were: David Berenbaum, National Community Reinvestment Coalition; Brian Brooks, O'Melveny & Myers, LLP; Luke Brown, Federal Deposit Insurance Corporation; Glenn Canner, Board of Governors of the Federal Reserve System; Jim Carr, National Community Reinvestment Coalition; Leonard Chanin, Board of Governors of the Federal Reserve System; Marsha Courchane, Charles River Associates; Eileen Harrington, Federal Trade Commission; Howard Husock, Manhattan Institute; Stan Liebowitz, University of Texas-Dallas; Ken Markison, Mortgage Bankers Association; Alfred Pollard, Federal Housing Finance Agency; Lisa Rice, National Fair Housing Alliance; John Weicher, Center for Housing and Financial Markets; and Barry Wides, Office of the Comptroller of the Currency. The briefing transcript, written statements, and oral testimony are cited herein and are available at www.usccr.gov.

Miscellaneous Other Research Efforts

In addition to information provided by the experts who briefed the Commissioners, the report relies on a select set of research not produced by federal agencies, most notably two studies of discrimination in mortgage lending. One is an academic piece by Marsha J. Courchane, and the other is from an advocacy group, the Center for Responsible Lending.[7] The Commission used these studies along with research by the Federal Reserve and its Boston and New York branches[8] in the credit scoring section. Notably, all five of these research efforts have very large samples of loans. They used proprietary industry data and census information, and, except for the historic Boston Fed study, combined such information with HMDA data. All employ complex statistical models using underwriting factors to adjust for differences in lending and pricing before attributing disparities to discrimination. Different results arise potentially because the New York Federal Reserve study is limited in the type of loans it examines[9] and the Center for Responsible Lending's analysis lacks loan pricing data for many of the mortgages as well as a measure of the borrower's debt.[10]

---

[7] Marsha J. Courchane, *The Pricing of Home Mortgage Loans to Minority Borrowers: How Much of the APR Differential Can We Explain?*, J. REAL ESTATE RES., vol. 29, no. 4 (2007), DEBBIE GRUENSTEIN BOCIAN, KEITH S. ERNST AND WEI LI, CTR. FOR RESPONSIBLE LENDING, UNFAIR LENDING: THE EFFECT OF RACE AND ETHNICITY ON THE PRICE OF SUBPRIME MORTGAGES 3 (May 2006).

[8] *See* Alicia H. Munnell, Lynn E. Browne, James McEneaney, and Geoffrey M.B. Tootell, *Mortgage Lending in Boston: Interpreting the HMDA Data* (Federal Reserve Bank of Boston, Working Paper No. 92-7, October 1992) or Alicia H. Munnell, Geoffrey M.B. Tootell, Lynn E. Browne, and James McEneaney, *Mortgage Lending in Boston: Interpreting HMDA Data*, AM. ECON. REV., vol. 86, no. 1 (March 1996); Board of Governors of the Federal Reserve System, *Report to the Congress on Credit Scoring and Its Effects on the Availability and Affordability of Credit*, August 2007; and Andrew Haughwout, Christopher Mayer, and Joseph Tracy, *Subprime Mortgage Pricing: The Impact of Race, Ethnicity, and Gender on the Cost of Borrowing,* Federal Reserve Bank of New York, p. 1, April 2009.

[9] Andrew Haughwout, Christopher Mayer, and Joseph Tracy, Federal Reserve Bank of New York, *Subprime Mortgage Pricing: The Impact of Race, Ethnicity, and Gender on the Cost of Borrowing,* staff report no. 368, April 2009, This study focused on one mortgage product—"2-28s," which have a fixed interest rate for the first two years and adjustable biannual resets in interest thereafter—and privately securitized loans. Ibid., pp. 3 and 8.

[10] Debbie Gruenstein Bocian, Keith S. Ernst and Wei Li, Center For Responsible Lending, *Unfair Lending: The Effect of Race and Ethnicity on the Price of Subprime Mortgages*, May 31, 2006, pp. 3 and 12–13.

STATEMENT OF VICE-CHAIR THERNSTROM

STATEMENT OF VICE-CHAIR THERNSTROM

August 20, 2009

Our nation finds itself in the midst of a massive financial and economic crisis that continues to have devastating consequences for mortgage holders of all races and ethnicities. This report seeks to at least partially answer a series of deceptively simple questions:

- What are the civil rights issues with respect to the mortgage crisis?
- Did long-standing policies to increase minority homeownership contribute to the crisis?
- On balance, did these policies hurt minority homeowners more than help them?
- If the effect of these policies has been to hurt minority homeowners, can the regulators point to civil rights violations that occurred either in the implementation or execution of these policies?
- During this period of economic turmoil, have the appropriate enforcement agencies been as vigilant as they could be in enforcing prohibitions against discrimination in mortgage lending?

What We Did Not Find: Perhaps it is easier to begin by stating what our report did not find.

Enforcement of Existing Anti-Discrimination Laws: Our report found no evidence that the myriad federal entities charged with prosecuting lending discrimination have failed to enforce lending discrimination laws. There are, however, a large number of such offices and no clear method of coordinating their efforts in a transparent, standardized manner. Monitoring and reporting on their enforcement efforts is thus difficult. Perhaps enforcement efforts would be more effective if communication and coordination among the various agencies were improved.

Credit Scoring and Minority Borrowers: Our report cites a landmark study by the Federal Reserve which found no evidence that, for any given credit score, minorities were rejected for loans or charged higher interest at rates that were different than those offered whites with the same credit score.[1] The Fed study concluded that credit scoring is not a proxy for the race or ethnicity of loan applicants. The study did note that some ethnic groups tend to have lower credit scores based on objective criteria such as ability to repay a loan. Neither the Federal Reserve study nor our report attempted to examine the historical, social and economic reasons that this is so.

Reduced Lending Standards to Promote Minority Homeownership: We did not find conclusive statistically significant evidence that regulatory mandates and policies to increase minority homeownership contributed to the current mortgage crisis. The best known of these mandates are the Community Reinvestment Act (CRA) and the Department of Housing and Urban Development (HUD) Lending Goals for Government Sponsored Enterprises (GSEs) such as Fannie Mae and Freddie Mac.

---

[1] "Report to the Congress on Credit Scoring and Its Effects on the Availability and Affordability of Credit", Board of Governors of the Federal Reserve System, August 2007. Submitted to the Congress pursuant to section 215 of the Fair and Accurate Credit Transactions Act of 2003. [Internet: http://www.federalreserve.gov/boarddocs/RptCongress/creditscore/creditscore.pdf. Last visited 8/15/09.]

Both programs sought to lower lending standards for the purpose of expanding minority homeownership. There is insufficient evidence to determine whether pressure for relaxed lending standards influenced the overall market.

Predatory Lending: The evidence that we collected for this report does not support the thesis that certain racial or ethnic groups were targeted by predatory lending schemes involving subprime loans. The bulk of subprime loans went to upper- and middle-income borrowers.[2] Our report notes that there is a lack of agreement among enforcement agencies and regulators about the definition of predatory lending. It is therefore not surprising that we found little enforcement activity in this area. By contrast, the collapse of the housing bubble has been accompanied by a sharp increase in prosecutions for mortgage fraud.

What We Did Find:

Rates of minority homeownership increased before and during the housing bubble, and even after the collapse of the housing bubble minority homeownership remains higher than it was previously.

From 1994 through 2005, overall ownership rates increased for the ethnic and/or racial subgroups examined. During that period, every minority racial or ethnic group showed stronger rates of growth than whites. Even following the collapse of the housing bubble, that remained the case.

Despite the growth of minority homeownership, and the narrowing of the gap between the various groups, substantial racial and ethnic disparities in homeownership rates remain. In 2008, the white homeownership rate stood at 71.7 percent, that of blacks at 47.4 percent, Hispanics at 49.1 percent, Asian/Pacific Islanders at 59.5 percent, and American Indians at 56.5 percent.

When credit history was taken into consideration, the denial of conventional mortgage applications narrowed. The gap between the denial rates of whites and blacks regarding refinance loans, however, did not close significantly.

Recommendations:

Federal efforts to increase homeownership within low- and moderate-income communities should take the form of direct subsidies, rather than regulatory mandates that contribute to weakened underwriting standards. The goal of federal assistance should be sustainable homeownership. That goal will require the use of more conservative underwriting standards. Such standards, at a minimum, should include: (1) a requirement that borrowers contribute some percentage of their own funds to down payments; (2) verification of income and employment that reflect an ability to pay the debts incurred; and (3) mandatory pre-purchase counseling for borrowers with credit scores below a minimum threshold.

---

[2] As our report notes on page 120 "Subprime lending is not synonymous with predatory lending. Subprime lending, in and of itself, simply reflects that some lenders are less creditworthy than others and, accordingly, pay higher interest rates or fees to obtain credit."

The landmark study by the Federal Reserve[3] provided an example of the depth and quality of data that should be routinely collected to assist in meaningful, standardized analysis of lending patterns and enforcement. At the time of the Fed study no comprehensive data set existed that allowed sorting lending data by credit score, loan cost and amount, rates of rejection, or by race, ethnicity and gender and other criteria that would be enormously useful. The study used Home Mortgage Disclosure Act (HMDA) data, supplemented with data collected from credit bureaus and other sources. Construction of this data set was time consuming and expensive and, to the best of our knowledge, data of this quality are still not collected in a routine, standardized way. Therefore, HMDA data should be revised to include credit score information, including the source of the system used. Additional suggested information would include: (1) fee and pricing standards for all loans, not just high-cost ones; (2) whether the loan was fixed and/or adjustable rate; (3) the length of time in which the initial rate is in effect; and (4) loan-to-value and debt-to-income ratios.

As noted, a large number of entities have responsibility for fair housing enforcement, but there is little coordination among them. Therefore, a federal inter-agency group should be utilized to coordinate fair housing enforcement policy for all federal programs, with transparent reporting on policy results. This action could occur through the President's Fair Housing Council or through a different entity. Any such committee should have as one of its primary goals the establishment of a uniform definition of those lending practices that constitute predatory lending and those acts that should be prohibited.

In the course of preparing this report we collected and analyzed an enormous amount of data from many regulatory and enforcement agencies. Meaningful analysis of potential civil rights issues arising from the mortgage crisis was hampered by differences in both the quality and type of data collected as well as by inconsistent enforcement policies taken by these agencies. I strongly recommend that additional studies be undertaken regarding racial and ethnic disparities in credit and the source of such disparities. Do they arise from legitimate issues of creditworthiness or from other factors? Exploring this issue would be greatly aided by the revised HMDA standards recommended above.

In the final analysis we have not been able to determine whether the mortgage crisis had a disproportionate impact upon minorities. Thus we cannot answer the important corollary question: If there was a disproportionate impact, is racial discrimination the explanation?

---

[3] See previous citation of the Federal Reserve study.

JOINT STATEMENT OF COMMISSIONERS MELENDEZ AND YAKI

JOINT STATEMENT OF COMMISSIONERS MELENDEZ AND YAKI

Because this report does not assess (or provide the underlying data necessary to assess) whether federal agencies have adequately enforced laws against mortgage lending discrimination, we could not approve this report. Much of the information in this report is useful, accurate, and provides a general background of federal jurisdiction and efforts to enforce mortgage lending laws. However, more is (and should be) expected of the only major annual report[1] of the U.S. Commission on Civil Rights ("Commission") on such a critical topic.

While the crisis in mortgage lending has affected all Americans, it has disproportionately hurt many minority homeowners and neighborhoods. Media reports and several court filings have identified discriminatory mortgage lending practices as a leading cause of minority homeowners' taking out high risk loans. In particular, there have been allegations of "steering," a practice by brokers and lending institutions of directing potential borrowers to apply for certain types of loans (e.g., subprime instead of prime) or to certain lenders (e.g., independent companies instead of regulated banks).

Such steering often occurs in the very first steps of a borrower taking out a mortgage, through targeted advertising, marketing, and bad advisory services. But the actions of lenders and brokers in these pre-application steps to a loan are not subject to the same regulatory review or reporting requirements that are triggered when a loan application is submitted. The Equal Credit Opportunity Act (ECOA) and Fair Housing Act (FHA) prohibit a lender from providing different information or services at any point in the lending process on the basis of a borrower's protected status (e.g., race, sex, or national origin). However, without implementing regulations that focus enforcement agencies' scrutiny of lenders' pre-application activities or expand lenders' disclosures of their activities, it is questionable whether the federal agencies responsible for enforcement of ECOA and FHA[2] have been monitoring steering enough.

A July 2009 report by the Government Accountability Office (GAO) entitled *Fair Lending: Data Limitations and the Fragmented U.S. Financial Regulatory Structure Challenge Federal Oversight and Enforcement Efforts* provides a useful assessment of the challenges faced by federal agencies trying to enforce ECOA and FHA prohibitions against steering and other discriminatory actions. GAO auditors not only conducted interviews of federal oversight agencies, but independently reviewed and analyzed the agencies' internal policies, past investigations, and even staffing. The report is available to the public on the GAO website at http://www.gao.gov/new.items/d09704.pdf and readers of this Commission report are strongly urged to turn to the GAO report for a more thorough, often clearer, examination of federal enforcement efforts regarding mortgage lending discrimination.

---

[1] By statute, the agency is directed to "submit to the President and Congress at least one report annually that monitors Federal civil rights enforcement efforts in the United States." 42 USC 1975a(c)(1). This annual report is the only deliverable specifically required of the agency by statute. Yet the agency has ceased initiating government-wide reviews of federal civil rights enforcement efforts in recent years. The agency's annual reports now attempt to focus on a narrower civil rights enforcement issue, yet even that goal has overwhelmed the agency's current capacity.

[2] While multiple agencies have FHA and ECOA enforcement authority over banks and savings and loans, the primary agencies with enforcement authority for these and independent nonbank lenders are the Department of Housing and Urban Development (HUD), the Department of Justice (DOJ), and the Federal Trade Commission (FTC).

In addition to noting the lack of lender reporting data that would enable more vigorous enforcement, the main findings of the July 2009 GAO report point to structural flaws in federal oversight:

> Federal oversight of lenders that may represent heightened risks of fair lending law violations is limited. For example, the enforcement agencies are responsible for monitoring independent mortgage lenders' compliance with the fair lending laws. Such lenders have been large originators of subprime mortgage loans in recent years and have more frequently been identified through analysis of HMDA data as outliers than depository institutions, such as banks. Depository institution regulators are more likely to assess the activities of outliers and, unlike enforcement agencies, they routinely assess the compliance of lenders that are not outliers. As a result, many fair lending violations at independent lenders may go undetected, and efforts to deter potential violations may be ineffective.
>
> Although depository institution regulators' fair lending oversight efforts may be more comprehensive, the division of responsibility among multiple agencies raises questions about the consistency and effectiveness of their efforts. For example, each regulator uses a different approach to analyze HMDA data to identify outliers and examination documentation varies. Moreover, since 2005, OTS [Office of Thrift Supervision], the Federal Reserve, and FDIC [Federal Deposit Insurance Corporation] have referred more than 100 lenders to DOJ for further investigations of potential fair lending violations, as required by ECOA, while OCC [Office of the Comptroller of the Currency] made one referral and NCUA [National Credit Union Administration] none.[3]

GAO auditors explicitly connect these informational and structural flaws of federal enforcement to the spike in risky loans made to minority homeowners in recent years. "Independent lenders, which were the predominant originators of subprime and other questionable mortgages that often were made to minority borrowers in recent years, generally are subject to less comprehensive oversight than federally insured depository institutions and represent significant fair lending risks."[4] "Second, limited data are available on the premortgage loan application process to help determine if loan officers engage in discriminatory practices, such as steering minority applicants to high-cost loans, before a loan application is filed."[5]

The GAO Report stops short of concluding that gaps in federal enforcement efforts allowed widespread discriminatory lending practices. However, the report makes clear that minority borrowers relied on loans that posed "significant fair-lending risks" and the extent of steering and other discrimination is unknown because of informational and structural defects in federal enforcement.

We support the GAO's conclusions and recommendations for remedial action, including increased reporting requirements for lenders, extension of the statute of limitations for ECOA, and interagency cooperation to identify approaches to better assess the potential risk for discrimination during the pre-

---

[3] Government Accountability Office, *Fair Lending: Data Limitations and the Fragmented U.S. Financial Regulatory Structure Challenge Federal Oversight and Enforcement Efforts* (GAO 09-704), July 2009, Coversheet.

[4] *Id.* at 63.

[5] *Id.* at 14.

application phase of mortgage lending. We hope that the GAO report, as well as some of the information in this Commission report, will spur Congressional and Executive branch action.

Unfortunately, this Commission report sheds little light on the extent and nature of federal enforcement, particularly when compared to the GAO report. There are many causes of this report's shortcomings. Elsewhere, we have noted the erosion of management and research standards for the agency's reports and this one is no exception. Agency written procedures were sidelined as deadlines were repeatedly overrun, state advisory committee input was not sought or included, inchoate drafts were presented for Commissioners' comments, and substantial changes were made to the plan originally approved by Commissioners without a Commission vote. Mid-stream, primary staff responsibility for this report was changed to the agency's Office of General Counsel (OGC) from the research division, the Office of Civil Rights Evaluation (OCRE). Staff cuts and poor management in the Commission's OCRE division have left it with just two social scientists, five staff overall, and an apparent inability to perform a major annual research project on its own. Finally, from its inception this report was saddled with a distracting directive from Commissioners to consider a misguided policy question—whether the Community Reinvestment Act (CRA) and other federal policies meant to aid minority homeownership contributed to the recent financial crisis and/or harmed minority homeownership.[6] For all these reasons, and despite the hard work of several agency staff, the present report has failed to meet the high standards for research that were once the hallmark of the Commission.

The national impact of the mortgage lending crisis, and the impact on minority homeowners in particular, has been staggering. As our country reviews and updates its regulatory structures and policies to prevent a similar occurrence happening again, leaders at all levels must take further steps to ensure that discriminatory mortgage lending practices end. A few years from now, after the wave of reforms has set in, we hope the Commission will be able to conduct a more careful review of whether federal enforcement of mortgage anti-discrimination laws has been effective.

---

[6] As the current mortgage crisis first arose a number of conservative academics suggested the CRA and other federal policies intended to promote minority homeownership had backfired and that these very policies were responsible in significant part for the present crisis. These critics claimed to find a causal link between legislation with minority homeownership goals, such as the CRA, and the relaxed credit lending standards that swept through the broader marketplace. Mainstream economists and federal regulators have since examined the matter and found that the CRA and the federal government's policies to promote minority homeownership are not significant causes of the current mortgage crisis. See Part I, Chapter 2 of the present report, above.

REBUTTAL STATEMENT OF COMMISSIONER MELENDEZ

REBUTTAL STATEMENT OF COMMISSIONER MELENDEZ

I join in the rebuttal statement of Commissioner Yaki, but also write to respectfully disagree with many of Vice-Chairperson Thernstrom's claims about what the report did and did not find. I also want to make clear to readers that the recommendations in the Vice-Chairperson's statement are not those of the Commission.

Unlike almost every other report issued by the Commission since 2005, this report has no findings and recommendations. No majority could be found to support the staff's draft findings and recommendations, or to put forward alternatives. Why? The report repackaged and highlighted some useful information gathered from other sources, but little more. The report's clear, one-sided evidence in Chapter 2 that the Community Reinvestment Act (CRA) did not play a significant role in the current mortgage crisis, for example, is hardly new.[1] This report and its underlying data are simply inconclusive about the many open questions that should have been tackled.

The Commission did not try to evaluate whether federal regulators were adequately enforcing lending discrimination laws (it just describes their jurisdiction and some of the few cases initiated in recent years). The Commission did not try to independently verify the conclusions of the 2007 Federal Reserve study about credit scoring (it just repeats its findings). Finally, the Commission did not try to collect evidence or evaluate whether minority groups were targeted by predatory lending schemes (although it describes some instances of fraud and lending discrimination that federal enforcement authorities investigated). Consequently, I disagree with the Vice-Chair's characterization that the Commission "did not find" problems with enforcement, credit scoring, or discriminatory predatory lending. In truth, the Commission never seriously looked into these questions at all.

One must look elsewhere to grapple with the extent of mortgage lending discrimination and federal enforcement. Again, for a review of the structural gaps in federal enforcement I strongly recommend interested readers review the July 2009 report by the Government Accountability Office (GAO) entitled *Fair Lending: Data Limitations and the Fragmented U.S. Financial Regulatory Structure Challenge Federal Oversight and Enforcement Efforts.* Several watchdog and advocacy organizations have also done helpful investigations and policy research on these issues, particularly the National Fair Housing Alliance. As Vice-Chair Thernstrom points out, there remains a need for more extensive research of these issues. However, academics, federal regulators, and enforcement agencies have struggled with the current limitations of the Home Mortgage Disclosure Act (HMDA) and Congressional action must be taken to expand HMDA reporting requirements if we are to get a system-wide picture of the extent of mortgage lending discrimination.

Lastly, while I generally support the Vice-Chair's interest in expanding HMDA data and increasing coordination of federal enforcement policy, I find the GAO's recommendations on these points more developed and useful. The Vice-Chair's call for direct subsidies to increase homeownership in low- and moderate income communities is interesting but was not a subject of study by the Commission. Also,

[1] This is the consensus position of academics as well as government experts. See, e.g., the Federal Reserve Bank of Cleveland's February 6, 2009 Conference on the Community Reinvestment Act, proceedings online at http://www.clevelandfed.org/research/Conferences/2009/2-6-2009/Proceedings.cfm.

contrary to the Vice-Chair's recommendation there is *no* basis in the agency's work to conclude that there should be a rollback of regulatory mandates as a means to encourage homeownership.

Our nation should consider all means at its disposal to address persistent economic and racial housing segregation, increase homeownership (particularly among minority populations), and enhance the effectiveness of lending anti-discrimination laws. Pragmatic solutions for our housing policy are needed to create the diverse, inclusive communities of economic opportunity that our country seeks.

REBUTTAL STATEMENT OF COMMISSIONER YAKI

REBUTTAL STATEMENT OF COMMISSIONER YAKI

I join in the rebuttal statement of Commissioner Melendez and wish to add the following.

The issue that was literally staring the Commission in the face, but which it chose not to touch, dealt with the issue of homeownership in minority communities. A recent study by the Pew Hispanic Center showed that gains in ownership in African-American and native-born Latino communities fell sharper than those in other communities during the current economic downturn.[1] The study also showed, as have other studies, that the gains in homeownership among minority communities between 1995-2004 was disproportionately tied to relaxed lending standards and subprime loans.

Interestingly, the Pew Report also showed interesting gaps, trends, and disturbing conclusions that the Commission Report barely acknowledged:

> Overall, the ups and downs in the housing market since 1995 have reduced the homeownership gap between whites and all racial and ethnic minority groups. However, a substantial gap persists. As of 2008, 74.9% of whites owned homes, compared with 59.1% of Asians, 48.9% of Hispanics and 47.5% of blacks.
>
> At the same time, blacks and Latinos remain far more likely than whites to borrow in the subprime market where loans are usually higher priced.2 In 2007, 27.6% of home purchase loans to Hispanics and 33.5% to blacks were higher-priced loans, compared with just 10.5% of home purchase loans to whites that year. For black homeowners who had a higher-priced mortgage, the typical annual percentage rate (APR) was about 3 percentage points greater than the rate on a typical 30-year, fixed-rate conventional mortgage; for Latinos who had a higher-priced mortgage, the typical rate was about 2.5 percentage points higher than that of the conventional mortgage.
>
> Moreover, in 2007, blacks and Hispanics borrowed higher amounts than did whites with similar incomes, exposing themselves to greater debt relative to their incomes. On both counts—the likelihood of higher-priced borrowing and higher debt relative to income—the gap between minorities and whites is greater among high-income households than among low-income households.[2]

The questions raised in the Pew Report merit further serious study. To summarize:

> (1) The persistent and substantial homeownership gap between whites and all racial/ethnic minority groups;
>
> (2) The interest rate and loan "type" gap between whites and racial/ethnic groups; and

---

[1] http://www.nytimes.com/2009/05/13/us/13homeowner.html

[2] Through Boom and Bust: Minorities, Immigrants and Homeownership, Rakesh Kochkar, Ana Gonzalez-Barrera, Daniel Dockterman, Pew Hispanic Center, May 12, 2009.

(3) The fact that the gaps persist even where incomes are comparable.

It is precisely these putative fact patterns and outcomes that are the raison d'être of the Commission. It is our mission to explore, understand, find facts and make recommendations where disparities in our society on the basis of race and ethnicity may persist. It does not mean, as some of the Commission majority doubtless fear, that it will necessarily result in more programs, regulations, or laws that would benefit a specific racial or ethnic group. But it may, but if so, that is for Congress and the Executive to debate and decide whether to enact a new law. Nevertheless, it does not serve our charter, does not benefit any group, nor does it contribute to our nation to ignore a potential issue and pretend it does not exist. Yet, sadly, the current Commission would rather direct its resources to destroy extant programs such as affirmative action, rather than to research current and persistent problems that affect our nation's commitment to equality and prosperity for all.

JOINT REBUTTAL STATEMENT OF COMMISSIONERS GAZIANO, REYNOLDS, KIRSANOW, AND TAYLOR

JOINT REBUTTAL STATEMENT OF COMMISSIONERS GAZIANO, REYNOLDS, KIRSANOW, AND TAYLOR

The Commission's 200-plus page report likely will speak for itself, regardless of what individual commissioners write about it. The initial statements of some other commissioners, however, deserve more attention, and in responding to them, we will refer to the report as well.

I. Scope and Coverage Issues

We tend to agree with Commissioners Melendez and Yaki that the scope of the last two statutory report projects seems, at least at times, to have "overwhelmed the agency's current capacity,"[1] but we draw different conclusions from that assessment than they do.

- The vacant staff positions noted in comments to last year's report are, due to budget constraints, still vacant. The Office of General Counsel and the Office of Civil Rights Evaluation are still operating at a fraction of their statutorily authorized strength. That suggests to us that we need to work harder to focus our resources on research questions: (i) that really matter, (ii) that are within our current capacity to properly analyze, and (iii) that are within our special mandate.
- The record of our proceedings reflects that some commissioners urged both staff and commissioners to narrow our study of the mortgage crisis and to do so early enough in the process so that we could produce social science of special significance. Indeed, commissioners reached an agreement early last fall that the topic would be narrowed as the staff work progressed and options were presented to us. Yet, at several important junctures, both staff and commissioners failed to follow through on this goal. Indeed, Commissioners Melendez and Yaki seemed interested in expanding the scope of the inquiry.
- Notwithstanding the failure to obtain data sources that may have produced more valuable original research, commissioners had ample opportunity to direct the staff's attention to particular issues of concern. Based on our discussion at Commission meetings, our staff was able to obtain witnesses who provided expert testimony and presented research on questions that several of us were interested in exploring. The expert testimony and related research shed light on whether certain minority-conscious federal policies may have contributed to a lowering of lending standards, and whether that, in turn, contributed to the home mortgage crisis. (See Part IV of this statement.)
- In contrast, Commissioners Melendez and Yaki never expressed an interest or concern with allegations of "steering" during our proceedings. Yet, they seem to fault the final report, in part, because it did not address whether some brokers and loan officers direct potential borrowers to apply for higher-cost loans. If Commissioners Melendez and Yaki were particularly interested in that topic, they should have said so before the final report was adopted.[2]

---

[1] Melendez and Yaki Joint Statement at note 1.

[2] There are many difficulties in evaluating steering allegations, especially as they relate to allegations of racially-biased steering (see below), but no commissioners asked for such an evaluation. Steering may be a subset of predatory lending, but

In short, commissioners should not complain that the final report did not contain a discussion of something if they did not express an interest in that topic, particularly with a subject as broad as the cause of the mortgage crisis, which will be debated in academic circles for years to come.

II. Quality Issues and the GAO Report

We agree with Commissioners Melendez and Yaki that "the information in [the instant] report is useful, accurate, and provides a general background of federal jurisdiction and efforts to enforce mortgage lending laws." As explained above, we also agree with them that this year's report could have been more valuable. But several of their criticisms—as well as the general tenor of their statement—are off base.

For example, Commissioners Melendez and Yaki compare a GAO report (issued in late July after the final draft of our report was circulated for approval)[3] favorably to our report, but it is not true that the GAO Fair Lending report is noticeably superior.[4] Though Commissioners Melendez and Yaki rely heavily on the GAO report in their statement on "steering" and other matters, the two reports do not have the same focus. Readers can judge for themselves the relative merits of the two reports, but we think both serve the public interest and neither tells the whole story.

III. The Lack of Evidence of Race-Based "Steering"

Neither the Commission's report nor the GAO report found statistical evidence of racial or ethnic discrimination in lending, or a failure by federal agencies to prosecute lending discrimination, which is the reasonable starting point to consider the "steering" allegation. Commissioners Melendez and Yaki admit there is no data to support claims that steering and other "pre-application activities" are a substantial problem. It's an even greater leap to assume racially-motivated steering is a problem. Nevertheless, Commissioners Melendez and Yaki call for increased reporting during the pre-application stage.

In many areas, minority borrowers are more likely to contact loan officers of the same race or ethnicity as themselves. Thus, in order to know whether race-based steering is taking place, it would be necessary to require the collection of data on the race/ethnicity of the broker, loan officer and every potential applicant. It is one thing to require such information on a loan application, but should the government really require brokers and loan officers to secure such personal information from every phone caller or internet rate inquiry? Even face-to-face contacts will not reveal the racial or ethnic background of many potential borrowers. Moreover, it would not be enough to know the race or ethnicity of all parties to a potential transaction. It would be necessary to know all the information that was exchanged in order to make some assessment regarding whether a particular pre-applicant was steered in the "right" or

---

as our report relates, the term "predatory lending" has no fixed meaning (other than as a pejorative) and encompasses many disparate notions. Indicating an interest in "predatory lending" is not specific enough.

[3] The final draft of the Commission's report was circulated to commissioners in mid-July and was approved on August 7, 2009. The GAO declined to make a copy of its report available to the Commission prior to our mid-July circulation date.

[4] If the acknowledgement page of the GAO report is an accurate guide, it also appears that the GAO may have devoted about three times the number of staffers to its report than the Commission could have.

"wrong" direction. There should be some reason to suspect racially-motivated steering is really a problem before recommending such an off-putting and potentially burdensome record-keeping regime.

A lack of data is not an indication of discrimination, but the bigger problem is that there is no logical or other reason to suspect discrimination at play in the pre-application process, especially when there is little or no evidence of discrimination in the rest of the loan process. Assuming *arguendo* that there was a significant amount of steering by mortgage brokers and lenders, there is no reason to suspect that mortgage brokers or lenders have a discriminatory motive to steer only minority borrowers (as opposed to all borrowers) to higher-cost products. Whether this is a manipulative practice that should be more heavily regulated or not, it makes no sense to think that race or ethnicity is a factor for those who engage in it.

By analogy, stock brokers have an incentive to steer all their clients to make trades that generate more and higher commissions, but there is no reason why they would do so only for clients of certain races or ethnicities. We suspect that the racial groups that comprise the upper-middle class pay more of these commissions, but that is only because they employ stock brokers more often. It has nothing to do with racial discrimination. Accordingly, there is no reason to require elaborate collection of data of the race of different stock market players. Likewise, neither the Commission's report nor the GAO's report contains sufficient evidence to support new record-keeping requirements for pre-application contacts in the mortgage lending industry.

IV. How Minority-Conscious Policies May Have Helped Cause and Exacerbate the Credit Crisis

As Vice Chair Thernstrom correctly points out, the report states that the data are inconclusive as to whether the Community Reinvestment Act (CRA) or the Department of Housing and Urban Development (HUD) affordable housing goals contributed to the mortgage crisis.[5] In their joint statement, Commissioners Melendez and Yaki point to some economists and federal regulators under fire who claim that "the CRA and the federal government's policies to promote minority homeownership are not significant causes of the current mortgage crisis."[6] Such self-serving claims, however, should not end the inquiry into whether and to what extent the CRA and other federal policies may have played a role in causing the mortgage crisis. Our report cites several other experts who make convincing cases that federal policies were major contributors to the crisis.[7]

Those who downplay the impact of the CRA cite the fact that only a small portion of failed loans were made by lenders subject to the CRA.[8] Professor Stan Liebowitz offered an interesting analogy to rebut

---

[5]AN EXAMINATION OF CIVIL RIGHTS ISSUES WITH RESPECT TO THE MORTGAGE CRISIS ("REPORT"), ch. 3, §§ V-VI.

[6] Commissioners Melendez and Yaki also claim that it was a waste of time even to investigate whether the CRA and other federal policies contributed to the mortgage crisis. Apparently, they would have avoided reviewing the major federal policies that explicitly sought to increase minority homeownership.

[7] *Id.* ch. 2.

[8] *Id.* ch. 2, § I (citing Press Release, Comptroller of the Currency, Comptroller Dugan Says CRA Not Responsible for Subprime Lending Abuses (Nov. 19, 2008), *available at* http://www.occ.treas.gov/ftp/release/2008-136.htm).

this point. Assume that a small group of sports car owners successfully lobbies to repeal all traffic lights and speed limits. Traffic laws are thus weakened. Chaos on the roads ensues, with traffic jams, increased accidents and injuries. When people blame the sports car owners, they point out that their sports cars comprise only a small portion of the cars involved in traffic jams and accidents. On that basis, they claim that they had nothing to do with the chaos on the roads.[9] Professor Liebowitz argued that the CRA and the HUD affordable housing goals contributed to the weakening of lending standards and thereby contributed to the mortgage crisis. This theory is worth exploring, and our report does so.

The Genesis of Weakened Credit Standards. The administrations of both Bill Clinton and George W. Bush set aggressive goals to increase homeownership in the United States, particularly for minorities and low-income individuals.[10] Part of the effort included encouraging lenders to weaken credit standards, such as by reducing down payment requirements and adopting more flexible loan policies.[11] Community groups such as the National People's Action on Housing pressured the federal government to weaken credit standards.[12] Federal policy resulted in substantial gains in home ownership, at least until the crash. Overall home ownership increased from 64 to 69 percent from 1994 to 2004. Black and Hispanic rates of home ownership increased more than that for whites during this period.[13]

However, the data suggest that weakening credit standards may not have been an effective means to increase home ownership for minorities in the long run. Conventional mortgage loans approved, as a percentage of conventional loan applications received, increased for all groups from 1999 to 2004, with blacks and Hispanics experiencing a greater increase than whites. But as the market tightened from 2004 to 2007, blacks and Hispanics suffered a greater decline in the rate of loan approvals than whites.[14]

Subprime mortgage data from 2004 to 2007 similarly show that weakening credit standards may have been counterproductive. Subprime mortgages increased dramatically for all groups from 2004 to 2005 and decreased dramatically from 2006 to 2007. Most minority groups, including blacks and Hispanics, received subprime mortgages at a higher rate than whites.[15] The foreclosure rate for subprime mortgages, always higher than for prime, rose dramatically from 2006 to 2008.[16]

The CRA and the HUD affordable housing goals certainly encouraged banks to weaken standards. In addition to the direct requirements imposed on CRA-covered banks, the CRA may have made it easier for banks with more aggressive, riskier lending policies to grow bigger through mergers and acquisitions relative to other banks with more prudent lending policies. This may be because the CRA requires federal bank regulators, such as the Federal Reserve and the Federal Deposit Insurance Corporation (FDIC), to take into account a bank's CRA record when evaluating the bank's application to merge with

---

[9] U.S. Commission on Civil Rights, Briefing Transcript at 53-54 (Mar. 20, 2009).

[10] REPORT, ch. 1, § I.

[11] *Id.*

[12] *Id.*

[13] *Id.* ch. 3, § I.B, fig. 3.1.

[14] *Id.* ch. 3, § II.A & fig. 3.3.

[15] *Id.* ch. 3, § III.A, figs. 3.9, 3.10.

[16] *Id.* ch. 3, § IV, figs. 3.11, 3.12.

or acquire another bank, or to open a branch in a new state.[17] In addition, federal bank regulators must consider comments and objections made by the public.[18] Public comments by community organizations and members of the public can have a substantial effect on regulators.[19] The danger to a bank that a federal regulator would turn down a proposed merger or acquisition based on CRA-type objections was real.[20]

To meet CRA requirements and avoid protests by community organizations, banks may have sought innovative ways to make loans to low-income borrowers in low-income communities. In a speech in 1998, Federal Reserve Board Governor Laurence H. Meyer noted concerns by "community development groups" that automated underwriting and credit scoring could result in "disparate impact discrimination."[21] To respond to these concerns, he urged banks to take advantage of new mortgage products in order to issue no-money down loans.[22]

Perhaps the most striking example of the conjunction between the CRA and aggressive lending practices was the case of Washington Mutual (WaMu). On December 21, 2001, WaMu announced approval from the Office of Thrift Supervision for its merger with Dime Bancorp.[23] In order to receive approval, WaMu made an unprecedented, $375 billion commitment to lend to low- and moderate-income borrowers.[24]

In late September 2008, the FDIC seized WaMu and sold its assets to JP Morgan Chase for $1.9 billion, despite WaMu purportedly having assets of $307 billion.[25] This was the largest bank failure in American history.

---

[17] 12 U.S.C. § 2903(a)(2); 2902(3)(E). Examining CRA requirements before blessing a merger or acquisition is the "stick" that helps regulators enforce CRA and keep the attention of regulated banks. Raymond H. Brescia, *Part of the Disease or Part of the Cure: The Financial Crisis and the Community Reinvestment Act*, 60 S.C. L. REV. 617, 633-34 (Spring 2009).

[18] 12 C.F.R. § 262.25.

[19] John Taylor and Josh Silver, *The Community Reinvestment Act at 30: Looking Back and Looking to the Future*, 53 N.Y.L. SCH. L. REV. 203, 206 (2008/2009).

[20] In 1993, the Federal Reserve initially denied Hartford, Connecticut-based Shawmut National Corporation's acquisition of New Dartmouth Bank of Manchester, New Hampshire, on the grounds of "possible lending bias." Steven Greenhouse, *Fed Stops Bank Merger: Cites Lending Concerns*, N.Y. TIMES, Nov. 17, 1993. The *New York Times* quoted one banking analyst, "'The Fed is sending a strong signal to the banking industry that they're going to be looking at banks' lending practices,' said Joseph Duwan, a banking analyst with Keefe, Bruyette & Woods. 'Clearly Shawmut is being made a little bit of scapegoat.'" *Id.* Shawmut certainly got the signal. It undertook an aggressive program to "increase lending activity to low-income Americans and minority groups that … [included] the use of more flexible income criteria." *Id.*

[21] Governor Laurence H. Meyer, Remarks Before the 1998 Community Reinvestment Act Conference of the Consumer Bankers Association (May 12, 1998).

[22] *Id.*

[23] Press Release, Washington Mutual, Washington Mutual Receives Regulatory Approval of Dime Acquisition (Dec. 21, 2001).

[24] *Id.*

[25] Madlen Read, AP Business Writer, *WaMu's Forced Sale Makes It Biggest U.S. Bank Ever to Fail*, Sept. 26, 2008, *available at* http://blog.cleveland.com/business/2008/09/wamus_forced_sale_makes_it_big.html.

Credit Scoring and Discrimination: The Harmful Impact of the Boston Fed Study. One alleged justification for loosening credit standards in the 1990s was the belief that credit scoring based on a traditional credit history discriminates against minorities. As Vice Chair Thernstrom noted in her statement, the report found no evidence that standard credit scoring is discriminatory. In fact, a Federal Reserve Board study from 2007 found that credit scores accurately predict risk for all major demographic groups. The study found that blacks and those living in lower-income and minority neighborhoods tend to underperform what their credit score would predict, while Asian-Americans and those living in higher-income neighborhoods tend to overperform what their credit scores predict. That is, the default rate for blacks was slightly higher than other races with the same credit scores, while the default rate for Asian-Americans was slightly lower.[26]

Yet, the Commission's report explains the serious, fatal flaws of an earlier (1992) study conducted by the Boston Federal Reserve Bank (BF).[27] That study had a profound influence on the public discussion and on policymakers, despite its invalidity.[28] Financial institutions "responded to the [BF study's] findings by making their underwriting criteria more flexible."[29] Until the early 1990s, the focus of bank regulators was on intentional discrimination. But the BF study "changed that, and attention has focused ever since on the issue of unintentional disparate treatment."[30]

Boston Fed Lending Guidelines. Perhaps the first policy change came at the BF itself when it published new lending guidelines, "Closing the Gap: A Guide to Equal Opportunity Lending," following the release of the study.[31] The purpose of the guidelines was to help "lenders as they work to close the mortgage gap" and as they "expand their markets to reach a more diverse customer base."[32] To reach more minority customers, the BF warned against "underwriting standards contain[ing] arbitrary or unreasonable measures of creditworthiness."[33] The guidelines suggested that lenders review their lending criteria, including standards relating to (1) the traditional obligation ratio, (2) down payments and closing costs, and (3) credit history.[34] On this last point, the task force stated:

---

[26] REPORT, ch. 5, § II.A.2.

[27] *Id.* ch. 5, § I.

[28] The *American Economic Review*, where the revised 1996 version was published, is widely regarded as the leading journal in economics. The study "had an enormous impact on the banking industry." Peter Passell, *Beyond Statistics: Study Doesn't Settle Issue of Why Minorities Lag in Mortgages*, CHICAGO TRIBUNE, May 18, 1996.

[29] Joseph M. Kolar and Jonathan D. Jerison, *The Home Mortgage Disclosure Act: Its History, Evolution, and Limitations*, 59 CONSUMER FIN. L. Q. REP. 189, 190 (Fall 2005). Richard Syron, who headed the BF when it performed and issued the study, was named chairman and chief executive of Freddie Mac in 1993. Syron was selected to head Freddie Mac, in part, because of his leadership in completing and issuing the BF study.

[30] *Shooting the Rapids of Credit Scoring and Fair Lending*, ABA BANKING J., Vol. 89, Issue no. 9, Sept. 1, 1997.

[31] FEDERAL RESERVE BANK OF BOSTON, CLOSING THE GAP: A GUIDE TO EQUAL OPPORTUNITY LENDING. The guidelines make reference to the BF study in the editors' note on page 2.

[32] *Id.* at 5.

[33] *Id.* at 13.

[34] *Id.* at 13-14.

> Policies regarding applicants with no credit history or problem credit history should be reviewed. Lack of credit history should not be seen as a negative factor. . . . In reviewing past credit problems, lenders should be willing to consider extenuating circumstances.[35]

Although these recommendations were only "guidelines," the publication ominously highlights the liability for lenders who fail to comply with federal housing laws. The message from the guidelines is clear: financial institutions must weaken their lending standards or they may face significant legal and financial exposure.

***HUD Interagency Task Force on Fair Lending*.** The BF study's influence was next felt in the major federal agencies with jurisdiction over fair housing laws. HUD led an Interagency Task Force on Fair Lending, which issued a "Policy Statement on Discrimination in Lending" on April 15, 1994.[36] The task force specifically cited the BF study as one of the reasons for its concern about discrimination in lending.[37] The purpose of the task force was "to establish uniform policy against discriminatory lending" because the federal agencies "share[d] a concern that some prospective homebuyers and other borrowers may be experiencing discriminatory treatment in their efforts to obtain loans."[38]

The HUD policy statement asserted that neutral lending policies which have a "disparate impact" on protected groups may be illegal.[39] HUD further argued that intent is not necessary to show illegal discrimination.[40] Once a disparate impact is identified, HUD maintained that the financial institution is illegally discriminating unless it can show that the "policy or practice is justified by 'business necessity.'"[41] The business necessity must be "manifest and may not be hypothetical or speculative."[42]

---

[35] *Id.* at 14.

[36] 59 Fed. Reg. 18266 (April 15, 2009). The task force members were representatives of HUD, the Department of Justice, the Department of the Treasury, the Office of the Comptroller of the Currency, the Office of Thrift Supervision, the Federal Reserve System, the Federal Deposit Insurance Corporation, the Federal Housing Finance Board, the Federal Trade Commission, and the National Credit Union Administration.

[37] *Id.* at 18267.

[38] *Id.*

[39] *Id.* at 18269. The policy statement is "based upon" two fair lending statutes, the Equal Credit Opportunity Act (ECOA) and the Fair Housing Act (FHA). *Id.* at 18267. Neither statute explicitly creates a cause of action based on disparate impact, but the courts have read such a cause of action into them. *See, e.g.*, *McDonald v. Coldwell Banker*, 543 F.3d 498, 505 n.7 (9th Cir. 2008) (FHA); *Golden v. City of Columbus*, 404 F.3d 950, 963 n.11 (6th Cir. 2005) (ECOA). The Supreme Court has never ruled on whether disparate impact claims are permissible under ECOA or FHA.

[40] 59 Fed. Reg. 18266, 18269.

[41] *Id.*

[42] *Id.*

Similar to the BF lending guidelines, the task force stated, "[L]enders should think critically about whether widespread, familiar requirements and practices have an unjustifiable disparate impact."[43] The message for financial institutions was that if a traditional lending policy has a disparate impact on minorities, the easiest path may be to weaken the policy. Otherwise, the financial institution may be challenged by federal regulators.[44]

HUD Affordable Housing Goals. The thinking that animated the BF study also influenced the affordable housing goals set for Fannie Mae and Freddie Mac by HUD, as described in Chapter 1, Section III, of our report. As noted above, HUD led the interagency task force warning financial institutions that their traditional lending standards may be illegal if they have a disparate impact on minority borrowers. HUD's affordable housing goals for Fannie Mae and Freddie Mac were one way to ameliorate this alleged discrimination. Increasing the number of loans in low-income areas and to low-income borrowers are indirect ways to increase loans to minorities and thereby reduce the alleged discrimination faced by minority borrowers, or so the thinking went. As discussed in the section on HUD's affordable housing goals, the requirement for loans bought by Fannie Mae and Freddie Mac going to low- and moderate-income borrowers rose from 30 percent in 1993 to 56 percent in 2008.[45]

Conclusion. The impact of minority-conscious federal programs on lowering lending standards and the subsequent default rate for minority and other borrowers may never be known with much precision. The Commission's study certainly did not attempt to quantify the possible impact. But the report sheds considerable light on possible causes that future scholars and public policy experts should pursue. It would be a mistake to ignore these leads just because the regulators themselves say that their policies had nothing to do with the mortgage crisis.

---

[43] *Id.* at 18269-18270.

[44] *See, e.g.*, Lawrence H. White, *How Did We Get into This Financial Mess?*, USA TODAY (MAG.), May 1, 2009 ("[B]eginning in 1993, officials in [HUD] began bringing legal actions against mortgage bankers that declined a higher percentage of minority applicants than white applicants. To avoid legal trouble, lenders began relaxing their down-payment and income qualifications.").

[45] REPORT, ch. 1, § III.C.

U.S. COMMISSION ON CIVIL RIGHTS

Washington, DC 20425

Visit us on the web: www.usccr.gov