Comments from Adam Rust, Research Director, Community Reinvestment Association of North Carolina

Federal Reserve Hearings on the Home Mortgage Disclosure Act
July 15th, 2010
Federal Reserve Bank of Atlanta

Governor and members of the CAC: Thanks for having me here today to talk about this important issue. In my job as a research director at the Community Reinvestment Association of North Carolina, I regularly work with HMDA data. Indeed, hardly a week goes by that I don't spend at least some time with HMDA, and there are some times when HMDA data takes up my entire week. All kinds of people approach me to help them answer questions with this data – from community groups, to other non-profits, to local municipalities, media, church organizations, foundations, and unions. Although there are some exceptions, their interest usually falls into one of two queries: Is there fair and equitable access to capital across their community, and are the prices and terms of loans reasonable? Their preference fluctuates with the pace of lending. Right now, with tight credit everywhere, most people want to know about access to credit. For the last few years, though, it was the other way around.

We need to update HMDA data because in the period since the last major update to the data, mortgage lending has changed. It isn't just a little difference, either. Most of the assumptions that could be made about mortgages in 1991 don't hold. We used to conceptualize all loans as a "good." More loans were good, and fewer loans were bad. Indeed, that assumption reflects the basic idea of the CRA. Now we have to think differently. Some loans are just not good. Our expectation for the attributes of those loans is also dated. At one point, most loans were originated with a fixed interest rate over a standard 30-year term, and the cost of the loan was fairly consistent. Now, we have exotic loans, hybrid option-ARM loans, negative amortizing loans, loans with balloon payments and prepayment penalties, and the rest. We used to expect that loans were made within a community, with a relationship that involved face-to-face interaction. Now, most loan decisions are a product of underwriting that incorporates credit scoring and prices loans based upon risk.

I'm not alone with this opinion. I've actually brought along some of the letters that banks have sent me. In each case, they are clear about their disdain for conclusions made from HMDA data. One lender put it this way: "*HMDA data also has serious shortcomings, as it does not include key financial information…important information might include credit score, property type, down payment, cash-out information, property value, debt-to-income ratio, loan-to-value ratio and assets.*"

They are saying that HMDA data needs to capture more data that bears relevance to underwriting. I would agree with them about the need for data can account for underwriting. I will add the HMDA data should be easy to use when possible, and that HMDA data should be published in as timely a fashion as possible.

Now, understand, there are some good things about HMDA data, too. Probably the most important aspect is that each row corresponds to one loan. Just think, by comparison, how many reports are made

with HMDA data and how few are made with small business loan data. We know that both are important, but the small business data is aggregated.

We can expect new data points in HMDA, thanks to language in the Dodd-Frank bill, and that is great. Still, the implementation is important. I would say that any data point that is aggregated, whether as an average over a census tract or as a median with an MSA, will lose most of its value.

HMDA data is a means for outsiders to add to the dialogue about lending in this country. If there had been more data to tell us about the extent of subprime lending, then more people would have been able to voice their concern about the issue. True, there were more than a few groups that did use HMDA data for this purpose, but often, they did that with the aid of additional data sources. Many purchased data from groups like McDash, First American Core Logic, and others. One of the shortcomings of that system is that we then have two groups of observers – the data "haves," and the data "have-nots."

I don't want to use this time to present a laundry list of items; it is clear to me that we'll have time to cover those in the question session later.

I do want to emphasize some principles that will matter for the general design of this data. For one, we need to pay attention to the ease of use. Too many people are challenged by HMDA, and they must resort to working through someone like me. Second, we need to have a better means of analyzing the quality of lending.

Going forward, I am worried about the implications for new policies at the GSEs. I feel that the Loan Level Pricing Adjustment (LLPA) will become a significant challenge for the kinds of borrowers that are meant to be served by the Community Reinvestment Act. The LLPA adds delivery charges to loans that are sold by lenders to the GSEs. It seems likely that these fees will be passed on to consumers. When they do, they will add costs to borrowing for low-income and minority households. The result will to limit access to credit and to exacerbate disparities in neighborhood reinvestment in low-and-moderate income communities.

Conclusion

I want to underscore the importance of improving HMDA, acknowledging that to date HMDA has been a powerful tool for supporting dialogue about neighborhood reinvestment. I recognize that any regulatory effort is tested by change and innovation in private markets. HMDA data is no different. We are faced with a challenge, but also with a need, to reconcile HMDA data with how mortgage loans are made today. HMDA data, as a free resource that is available to the public, is an important element for making sure that communities can gain access to capital. It can also be a beacon to warn about the Fire Next Time – if there is another crisis like the one we just experienced – and for that, any contribution is time well-spent. Thanks for your concern about this issue.