A Principle-Based Redesign of HMDA and CRA Data

Adam Rust
Community Reinvestment Association of North Carolina

Community groups rely on the Home Mortgage Disclosure Act (HMDA) and the Community Reinvestment Act (CRA) databases to engage in advocacy. Those databases, however, have not kept up with recent financial innovations, particularly in subprime mortgage lending, and need to be reformed.

The authors of the Community Reinvestment Act of 1977 emphasized regulation through standards. It was a "hands-off" approach: on the one hand, banks could decide for themselves how most efficiently to design plans for fulfilling their local lending obligations, but, on the other, citizens had a right to know if depository institutions were fulfilling the housing needs of their communities.[1]

Armed with data from the HMDA and the CRA databases, users (consumer advocates, regulators, state attorneys general, municipalities, and reporters) have been active as monitors or advocates.[2] These same groups now find their reach limited by the mismatch between existing data and new financial products.[3]

The challenge facing policymakers is to adopt a principle-driven data standard that meets users' needs. Such a redesign should be relevant, universal, and substantive. *Relevant*, in an era after subprime innovation, means updating the data to account for new permutations in lending. *Universal* means that there are accepted definitions for data variables, both in the scope of their coverage and in how those numbers are calculated, so that all financial institutions report in the same way. *Substantive* means that it helps users to monitor lenders in fulfilling the requirements of the CRA. Substantive data contribute to answering questions about the fulfillment of credit across geographies, across income levels, and with respect to the race and ethnicity of borrowers.

These principles hew to the original legislative intent of the CRA. Policymakers should ask if data, as they are collected and distributed, currently serve that purpose. This is the appropriate lens for evaluating how well implementation of the CRA lives up to the intent of the law.

Data Shape the Dialogue

As one commenter put it, "We have learned from 30 years of CRA policy that what is measured gets done."[4] The fact that policy discussions have focused mainly on home mortgages reflects well on the HMDA data relative to the CRA data.

In a standards-based system, data are vital to enforcement. Most alternatives to the existing standards system would rely less on public access to data. Numerical targets, established through negotiation between banks and regulators, would not require public participation.[5] A cap-and-trade system, where banks could choose between making loans or buying credits, would also skirt input, particularly in communities where lending to low-income communities was deemed relatively less efficient.[6] A system of direct subsidies for community

1 12 U.S.C 2801 et seq., 89 Stat. 1125, Pub. L. 94-200 (1975).

2 Allen J. Fishbein, "The Ongoing Experiment with 'Regulation from Below': Expanded Reporting Requirements for the HMDA and CRA," *Housing Policy Debate* 3(2) (2003): 601–36. See also: Allen J. Fishbein, "The Community Reinvestment Act after Fifteen Years: It Works, But Strengthened Federal Enforcement Is Needed," *Fordham Urban Law Journal* 20 (1992): 293–310; Malcolm Bush and Daniel Immergluck, "Research, Advocacy, and Community Investment," in *Organizing Access to Capital: Advocacy and the Democratization of Financial Institutions*, ed. Gregory D. Squires (Philadelphia: Temple University Press, 2003), 154–68.

3 Richard Neiman, Testimony on behalf of the New York State Banking Department, Committee on Banks, Subprime Mortgages and Foreclosures in New York. New York State Senate, December 13, 2007.

4 Ellen Seidman, New America Foundation. Testimony before the Committee on Financial Services, U.S. House of Representatives, 2008, available at http://www.newamerica.net/files/CRA%20Testimony%202-13-08.pdf.

5 Peter Swire, "Safe Harbors and a Proposal to Improve the Community Reinvestment Act," 79 Virginia law Review 349.

6 Michael Klausner, "Letting Banks Trade CRA Obligations Would Offer Market-Based Efficiencies," American Banker, January 21, 1994, 26.

development and mortgage lending, paid for by general tax revenues, would shift the debate to government budget committees.[7]

The conversation surrounding the accommodation made by financial institutions to their communities has followed the evolution of the content of these databases. The original HMDA-based analyses were characterized as "redlining studies" that focused on the aggregate flows of capital into neighborhoods.[8] They focused on access to capital and less so on the terms of credit.[9] For example, analysts related lending volume in census tracts to the share of housing units in those tracts. When critics found fault with those studies, they pointed out that missing variables that were significant in underwriting might explain gaps in credit allocation: credit risk, demand for mortgage loans, and measures of equity.[10]

The Financial Institutions Reform, Recovery, and Enforcement Act of 1989 (FIRREA) amended the rules to reveal more demographic information about borrowers. The act moved the focus away from redlining of whole communities and toward discrimination against individual borrowers. The Federal Financial Institutions Examination Council (FFIEC) amended the structure of the HMDA database to provide loan-level data, including recordkeeping for credit denials. Congress sought to link lending to LMI and minority borrowers, both on the individual and community level, as a *quid pro quo* for bailing out the failed savings and loan industry. FIRREA established authority for HMDA reporting to monitor lending in low-income and minority communities.[11]

The new data structure established a "golden age of the CRA."[12] The interplay of new variables (race, income, loan decisions) within loan-level data allowed analyses that until then had been set aside.[13] Community groups were emboldened to pursue their goal of "regulation from below." They could back up their assertions about neglect in low-income neighborhoods with relevant data. Studies identified that demand did exist for loans, but that credit was often denied.[14] Observers noted that community groups simultaneously "grew up, focusing less on confrontation and more on tangible results."[15] More than 300 "lending agreements" were signed.[16] Meetings, coinciding with the release of new data, focused on monitoring the extension of credit.[17]

Data remained relevant, and thus valuable, through the 1990s. After the Riegle-Neal Interstate Banking and Branching Efficiency Act of 1994, mergers led to a set of very large banks. Community groups and large cities, as well as some media, used HMDA and CRA data to influence the approval process.[18] Banks responded proactively to the new environment. Many created community development departments to guarantee investment across their local communities.[19]

Although a change in 2005 offered interest-rate data on higher-cost mortgage loans, the value of HMDA and CRA data are now challenged; first, by the availability of

7 *Jeffrey Lacker, "Neighborhoods and Banking," Economic Quarterly 81(2) (1995): 13–38.*

8 *Kavous Ardalan, "Community Reinvestment Act: Review of Empirical Evidence," Academy of Banking Studies Journal 5(1) (2006): 25-42.*

9 *Ibid.*

10 *Mark Sniderman, "Issues in CRA Reform," Economic Commentary, Federal Reserve Bank of Cleveland, March 1, 1994, available at http://www.clevelandfed.org/Research/commentary/1994/0301.pdf.*

11 *Patricia A. McCoy, "The Home Mortgage Disclosure Act: A Synopsis and Recent Legislative History," Journal of Real Estate Research 29(4) (2007): 391–98.*

12 *Fishbein, "The Ongoing Experiment with 'Regulation from Below,'"601–36.*

13 *McCoy, "The Home Mortgage Disclosure Act," 391–98.*

14 *Alicia H. Munnell, Geoffrey M. B. Tootell, Lynn E. Browne, and James McEneaney, "Mortgage Lending in Boston: Interpreting the HMDA Data," American Economic Review. Working Paper 92-7 (1996), Federal Reserve Bank of Boston.*

15 *Gregory D. Squires, "Introduction: The Rough Road to Reinvestment," in Organizing Access to Capital: Advocacy and the Democratization of Financial Institutions, ed. Gregory D. Squires (Philadelphia: Temple University Press, 2003), 1–26.*

16 *Raphael Bostic and Breck Robinson, "Do CRA Agreements Influence Lending Patterns?" Real Estate Economics 31(1) (2003): 23–51.*

17 *Alan Schwartz, "From Confrontation to Collaboration? Banks, Community Groups, and the Implementation of Community Reinvestment Agreements," Housing Policy Debate 9(3) (1998): 631–62.*

18 *Ibid. See also: B. Dedman, "The Color of Money," Atlanta Journal-Constitution, May 1988, 1–4.*

19 *Ben Bernanke, "The Community Reinvestment Act: Its Evolution and New Challenges," Speech given at the Community Affairs Research Conference, Washington, DC, March 30, 2007.*

better products from private vendors; and second, by a sense that the data are less relevant.[20] HMDA does not capture many characteristics of subprime loans, a set of products that has substantially increased in volume,[21] particularly within underserved markets.[22] In 2007, for example, the leading provider, by loan amount, of non-high-cost mortgage loans to LMI borrowers was Countrywide Financial.[23] The data present a false positive. Users know that the lender issued more than $96 billion in adjustable-rate mortgages in the same year, but they have no alternative data source to describe more fully the impact on communities.[24]

Subprime lending is not about "access to credit" as much as it is about terms of credit. Subprime loans have increased opportunities for homeownership among low-income borrowers. Still, these loans concern policymakers because of "troubling reports of abusive and unscrupulous credit practices, predatory lending practices, which can strip homeowners of the equity in their homes and ultimately even result in foreclosure."[25]

The data's demise occurs at a time when community groups and the regulation of the larger mortgage market are troubled. Lending agreements are now infrequent. Anecdotal evidence suggests that credit needs are still going unmet by banks and thrifts. In low-income neighborhoods, a different set of fringe lenders (payday lenders, pawnshops, check cashers) often supply the bulk of financial services. Some assert that the CRA cannot function without more room for community groups to participate.[26]

The divergence of HMDA and CRA data from the innovation in the marketplace at a time of disruption in normal lending suggests that policymakers should examine how to modernize the data sets.

Countering the Critics

Data collection is itself the subject of much controversy within the dialogue surrounding the implementation of the Community Reinvestment Act. Critics of HMDA and the CRA contend that the costs of collecting and reporting data, when underwriting and credit scoring already identify opportunities in low-income geographies, is inefficient, expensive, and especially onerous to small banks.[27]

To be sure, tangible costs are associated with geocoding loans, hiring compliance officers, and doing paperwork. Still, a 1999 study estimated that a large bank would spend only about 600 hours of staff time per year to fulfill the rules.[28] The burden of reporting is easily relieved by data products already available in the marketplace. Private vendors have created data systems to aid financial institutions with reporting.

Some financial institutions have argued that distribution of HMDA and CRA data forces them to compromise the privacy of their clients.[29] There is some truth to this. The data sets do contain explicit information that reveals quite a lot when appended with other data sets. But

20 *Richard Neiman, Testimony on behalf of the New York State Banking Department, Committee on Banks, Subprime Mortgages and Foreclosures in New York, New York State Senate, December 13, 2007.*

21 *Michael Staten, "The New HMDA Pricing Data: What Can It Tell Us about Pricing Fairness?" Testimony before the U.S. House of Representatives Committee on Financial Services, Subcommittee on Financial Institutions and Consumer Credit, June 13, 2006.*

22 *Richard Williams, Reynold Nesiba, and Eileen Diaz-McConnell, "The Changing Face of Inequality in Home Mortgage Lending," Social Problems 52(2) (2005):181–208.*

23 *Federal Financial Institutions Examination Council, Home Mortgage Disclosure Act Database.*

24 *Countrywide Financial Corporation, SEC Form 10-K for year ended December 31, 2007, 65.*

25 *Remarks by Governor Edward M. Gramlich at the Community Affairs Research Conference of the Federal Reserve System, Washington, DC, April 5, 2001.*

26 *Raphael W. Bostic and Breck L. Robinson, "Do CRA Agreements Influence Lending Patterns?" Real Estate Economics 31(1) 23–51.*

27 *Jonathan Macey and Geoffrey Miller, The Community Reinvestment Act: An Economic Analysis, 79 Virginia Law Review 291 (1993). See also: Olaf de Senerpont Domis, "Truth-in-Lending, CRA Makes '10 Worst Rules' List," American Banker, January 31, 1995, 3; George Bentson, "It's Time to Repeal the Community Reinvestment Act," Cato Institute, Washington, DC, 1999, available at http://www.cato.org/pub_display.php?pub_id=4976; and General Accountability Office, "Race and Gender Are Limited for Non-Mortgage Lending," GAO-08-698, June 2008, available at http://www.gao.gov/new.items/d08698.pdf.*

28 *OMB Review, 64 Fed. Reg. 29,083, 29,084, 29,086 (Treasury Department, May 28, 1999).*

29 *William Apgar and Mark Duda, "The Twenty-Fifth Anniversary of the Community Reinvestment Act: Past Accomplishments and Future Regulatory Challenges," Paper presented at the conference Policies to Promote Affordable Housing, co-sponsored by the Federal Reserve Bank of New York and New York University, February 2002.*

these cries ring false in the greater context of "business as usual" practices. If banks were sincere in their desire to safeguard the financial information of their customers, they would not sell data to third parties. In 1999, privacy groups estimated that most Americans appeared in between 25 and 100 databases.[30] Financial institutions share and sell information to marketing groups or to third parties.

HMDA is a limited data set for groups without financial resources to pay for better information. A set of data providers (Loan Performance, First American CoreLogic, FiServ, Fitch Ratings, Case-Shiller, McDash Analytics) buy loan-level home mortgage data and then repackage the data for consumption by other lenders, analysts, and academics. Some nonprofit groups buy this information, but for the most part, it is too expensive for them.

Changes in Mortgage Lending Support Changes in HMDA Data Reporting

While many important questions can be asked about HMDA, more than a few observers point out that important criteria in underwriting are largely ignored by the HMDA data. A chorus of voices regularly attempts to characterize any claims generated from HMDA data as dubious. One senior vice president of a West Coast bank put it this way in a letter replying to a request for HMDA data: "Please also consider that the HMDA results tell only part of the story, since certain risk and other loan factors that affect pricing are not included."[31] The FFIEC concurs, observing that HMDA data lack information in important areas: credit history, debt-to-income ratio, and loan-to-value ratio.[32]

To shore up relevancy, some assumptions that drive the CRA need to be updated. Notions about underwriting were derived prior to credit scoring.[33] Internet and telephone applications, which are often taken through mortgage brokers, have weakened the link between branch banking and mortgage lending.[34] Only a small minority of loans are originated by covered lenders in their assessment areas.[35]

"Regulation from below" will be enhanced by new data that can track new features in lending, including characteristics of subprime loans. Table 1 lists new variables, or modifications to existing variables, that would match HMDA data to modern financial products.

The variables in Table 1 can help users in a variety of ways. Some will make the HMDA data sensitive to loan products with subprime characteristics. Some will help users test the safety and soundness of underwriting by identifying loans where borrowers will be challenged to make their payments. Some, like age, would help to monitor extension of credit to prohibited bases protected by the Equal Credit Opportunity Act.[36] Others, if used as independent variables (property type, owner occupancy), will reduce unexplained variations in loan pricing or access to credit. Data on down payments would fulfill a critique first recognized in 1961 by the U.S. Commission on Civil Rights.[37]

Those improvements would be aided by a complementary effort to ensure that current data reporting rules are observed. The second most frequent racial identity in 2001 was "information not provided."[38] Loan-denial data remain voluntary.

30 *Andrew Shapiro, "Privacy for Sale: Peddling Data on the Internet," Human Rights 26 (1999): 10.*

31 *Letter to the author. Lynn Greenwood, senior vice president, Home and Consumer Finance Group, Wells Fargo, July 30, 2008.*

32 *Federal Financial Institutions Examination Council, Press Release, September 11, 2008. At http://www.ffiec.gov/hmcrpr/hm091108.htm.*

33 *Hollis Fishelson-Holstine, "Credit Scoring's Role in Increasing Homeownership for Underserved Populations," in Building Assets, Building Credit, ed. Nicole Paul Retsinas and Eric S. Belsky (Washington, DC: Brookings Institution Press, 2005), 173–202. See also: R. E. Litan, N. P. Retsinas, E. S. Belsky, G. Fauth, M. Kennedy, and P. Leonard, "The Community Reinvestment Act After Financial Modernization: A Final Report," U.S. Department of the Treasury, 2001.*

34 *Joint Center for Housing Studies, "The Community Reinvestment Act: Access to Capital in an Evolving Financial Services System." Report prepared for the Ford Foundation, March 2002. From a pdf viewed at http://www.jchs.harvard.edu/publications/governmentprograms/cra02-1.pdf.*

35 *Ibid.*

36 *15 U.S.C. 1691; Regulation B, 12 CFR 202, section 202.2(z).*

37 *1961 U.S. Commission on Civil Rights Report (Washington, DC: United States Commission on Civil Rights, 1961).*

38 *E. K. Wyly and S. R. Holloway, "Invisible Cities: Geography and the Disappearance of Race from Mortgage Lending Data in the USA," Social and Cultural Geography 3(3) (2002): 247–82.*

Table 1: Some Substantive Improvements to the HMDA database

Variable	Outcomes	Relevant?	Uniform?
LOAN			
Loan-to-value	Loan amount to loan appraisal	Cash-out	Yes
Debt-to-income	Annual PITI (post-reset)/annual income	Ability to repay	Yes
Down payment	Money down (percent of price or loan amount)	Underwriting	Yes
Reset	Identify year of reset, or specify “fixed”	Clarity	Yes
Loan term	Less than 20, less than 30, or more than 30 years	Clarity	Yes
Loan purpose	Expand to include HELOCs and reverse mortgages	Predatory	Yes
Owner occupancy	Expand to include second home (non-investor)	Transparency	Maybe
Principal repayment	Negative amortization, interest-only, and/or balloon	Subprime	Yes
Escrow taxes/insurance	Yes/no	Ability to repay	Yes
Prepayment penalty	Yes/no	Subprime	Yes
Property type	Differentiate between personal and real property for manufactured housing	Clarity	Yes
Transaction Cost	If closing costs/loan amount >2 percent	Subprime	Maybe
Income	Expand to include stated income	Subprime	Yes
Piggyback loan	Explicit: yes/no, or no with PMI	Soundness	Maybe
BORROWER			
Age	Under 24, 25 to 39, 40 to 49, 50 to 59, 60+	Predatory	Yes
LENDER			
Channel	Broker, correspondent, bank, wholesale	Transparency	Yes

Updates to CRA Small-Business Data

Any observation about how to improve the CRA data begins from a dramatically different starting point. The CRA database does not use loan-level reporting. It also fails to account for the heterogeneity in business lending, and it allows subsidiaries of banks to avoid reporting on activity.

Small business lending activity lacks the standardization that exists in mortgage lending, and it is often more complicated. Amendments to data could clarify some of the instances where current reports appear vague. The CRA data set should be redesigned to meet the needs of community groups. Users want small business data that will answer questions about lending geography, as well as about the nature of the borrowers being served.

A small business CRA database built on a loan-by-loan level would transform the CRA, just as loan-level data previously transformed the power of HMDA data after FIRREA. The impact would be further enhanced by reporting on all actions with loan decisions. The following variables, if incorporated in loan-level format, would make that difference.

The apples-and-oranges nature of lending can be muted. Specific variables could help users categorize loans and businesses. Risk is very different among different business types. The North American Industry Classification System (NAICS) provides uniformly interpretable business typologies that would serve this need.

For loan terms, consider that more than one in four small businesses use a business credit card.[39] Yet, the

39 *National Survey of Small Business Finances, 1998.*

CRA does not distinguish between a credit card, a line of credit, and a complicated small business loan. A loan term variable could make this distinction. There also must be clarification of the following: degree of collateralization, the term of the loan, and loan characteristics.

Table 2 reflects the same principles that drive the agenda for reforming HMDA data. The new variables are both relevant and universal. They are relevant because they are important underwriting factors. Many come from the Small Business Administration's explanation of how it makes credit decisions.

These possible improvements would strengthen the ability of users to gauge how institutions are lending. The data would have wide use, given the connection between small business lending and job creation.

Job creation has been an important focus of community development since the Great Depression, yet those figures are not currently captured in CRA data.[40] "The principal goal of local economic development," it has been said, "is to stimulate local employment."[41] NAICS data, combined with loan amounts, suggest likely job benefits for users with input-output software. A job-creation variable would be useful for groups without access to input-output analysis.

The need to have race data is traditionally challenged by the corporate nature of borrowers. What corporation has a race or gender? SBA minority- and woman-owned designations already exist and provide an incontrovertible means for reporters to identify their business. An ongoing challenge to uniform interpretation is determining the location of a loan.

Community development lending could itself be enhanced by loan-level data reporting. Current reporting meets none of the principles outlined earlier.

Table 2: Small Business Lending Variables

Variable	Outcomes	Relevant?	Uniform?
LOAN			
Loan purpose	Capital expenditure, inventory, working capital	Heterogeneity	No
Loan decision	Originate, approve, deny, incomplete	Fair lending	Yes
Loan term	Categorical term length, or line of credit	Heterogeneity	Yes
Collateralization	Equity, real property, inventory, personal, other, none	Heterogeneity	Yes
Loan amount	Specify amount	Clarity	Yes
BORROWER			
Business type	Three-digit NAICS classification	Heterogeneity	Yes
Debt to equity	Liabilities/equity	Ability to repay	Yes
Working capital	Current assets/current liabilities	Ability to repay	Yes
Owner designation	Identify minority- or female-owned business	Fair lending	Yes
Revenue	Maintain in new database	Ability to repay	Yes
Franchisee	Yes/no	Management	Yes
Firm size	Categorical indicator of number of employees	Job creation	Yes
Firm experience	Categorical indicator of firm tenure	Job creation	Yes
Job creation	No, or quantity of jobs	Job creation	Yes

40 Jonathan R. Kesselman. *"Work Relief Programs in the Great Depression." In Creating Jobs: Public Employment Programs and Wage Subsidies, edited by John L. Palmer, (Washington, D.C.: Brookings Institution, 1978).*

41 *Edward J. Blakely and Ted K. Bradshaw, Planning Local Economic Development: Theory and Practice (Thousand Oaks, CA: Sage Publications, 1990), xvi.*

Financial institutions differ in their reporting of the data. The first step would be to break down reporting to the individual loan; next, attach basic descriptions of loan terms; and finally, add demographic information where possible.

Conclusion

The CRA's standards-based system must have useful data. These proposed data changes will bring HMDA and the CRA up to date with the new marketplace. The existing acts (HMDA, CRA, FIRREA) show us that data have a place in helping the public and regulators determine the extent to which financial institutions are serving the credit needs of their communities. The current credit crisis makes clear the need for these data. If this article had been written one year ago, it would have emphasized the eclipse of "access to credit" issues by "terms of credit" issues. In that paradigm, getting loans was a concern of the 1980s and 1990s. A year ago, the task of a community group was to warn consumers against the dangers of easy subprime loans. The data need to be updated to understand those products, particularly in the mortgage markets, but new challenges add to that expectation.

Once again, public concern is focused on access to credit. The lack of liquidity makes it more apparent that CRA data need to be enhanced. The lack of credit for small businesses is a compelling public policy problem.

Some unprecedented mergers also have regulatory implications. Three large megabanks (Bank of America, Wells Fargo, and JPMorgan Chase) collectively hold 32 percent of national deposits.[42] For consumer advocates, there has never been a time when the David-and-Goliath nature of the field was more evident. All three institutions have Outstanding CRA evaluations. And although some may take that as a verdict on their service to communities, it remains true that JPMorgan Chase and Bank of America have acquired some of the nation's largest subprime lenders (Washington Mutual and Countrywide). Moreover, both these institutions and their recent investment bank acquisitions (Merrill Lynch and Bear Stearns) all had healthy appetites for subprime loans on the secondary market in recent years.

History has set a precedent. FIRREA's reforms were prompted by the savings and loan crisis. There was a time when the idea that community investment was a *quid pro quo* attendant with FDIC insurance.[43] Taxpayer investment, as structured by the Troubled Assets Relief Program (TARP), potentially moves the debate back to that place and perhaps further.

The makeup of HMDA data was last revised in 2005. The last substantial change took place after FIRREA. While CRA data have remained in their current form since 1995, I have attempted to show how the data lag behind the marketplace. Today, there is a new awareness of the importance of lending among the public. For policymakers, this should represent an opportunity to restore the role of research and advocacy within the "regulation from below" that marked the best of the implementation of the CRA. ■

Adam Rust is research director for the Community Reinvestment Association of North Carolina. Rust earned a master's degree in City and Regional Planning from the University of North Carolina at Chapel Hill in 2003, a master's degree in Journalism from the University of Missouri-Columbia in 1997, and a BA in History from the George Washington University in 1992. He is the author of This is My Home: the Challenges and Opportunities of Manufactured Housing. The book combines photographs and policy analysis exploring how nonprofits can reinvent manufactured housing to fit within the mission of providing affordable and secure shelter for working families.

42 *Eve Tahmincioglu, "Just 3 'Superbanks' Now Dominate Industry," MSNBC.com, available at http://www.msnbc.msn.com/id/27441147.*

43 *Jonathan Brown, "Community Benefit Requirements for Banking Institutions: The U.S. Experience," (Washington, DC: Essential Information/Banking Research Project, 1991).*