

3-1-2003

Introduction to Reflecting on the Legal Issues of our Times: New York Law School Faculty Presentation Day

Richard A. Matasar
New York Law School

Follow this and additional works at: https://digitalcommons.nyls.edu/fac_articles_chapters

Recommended Citation

46 N.Y.L. Sch. L. Rev. 3-4

This Article is brought to you for free and open access by the Faculty Scholarship at DigitalCommons@NYLS. It has been accepted for inclusion in Articles & Chapters by an authorized administrator of DigitalCommons@NYLS.

SUBPRIME LENDING, PREDATORY LENDING, AND THE COMMUNITY REINVESTMENT ACT OBLIGATIONS OF BANKS

RICHARD D. MARSICO*

INTRODUCTION

The last several years have seen tremendous growth in the subprime home mortgage lending industry. Broadly defined, subprime loans are loans available on more expensive terms to borrowers who have weak credit histories or repayment abilities. The growth of the subprime lending industry has also spawned growth in a pernicious sub-category of subprime lending, known as predatory lending. Predatory loans are characterized as loans with abusive terms, deceptive practices, and the inability of a borrower to repay the loan. The growth of subprime and predatory lending has prompted an important question about the Community Reinvestment Act ("CRA"): What is the relationship between subprime and predatory lending and a bank's obligation under the CRA to meet the credit needs of its community?

In order to analyze subprime lending, predatory lending, and the Community Reinvestment Act ("CRA") obligations of banks, it is helpful to examine the three purposes of the CRA: to encourage banks to make more loans in their local communities (and in particular in low- and moderate-income neighborhoods within their communities); to make sure that the loans meet the credit needs of their communities, ("meet the credit needs" meaning meeting both the demand for loans and the needs of the borrower); and to meet the credit needs in a way that is consistent with safe and sound banking practices.

With these three purposes of the CRA in mind, it is clear predatory lending has no role to play in satisfying a bank's CRA obligations. Predatory lending does not meet the credit needs of borrowers and is unsafe and unsound lending. Whether subprime lending should help a bank satisfy its CRA obligations to meet the credit needs of its community is a somewhat more complex issue. On the one hand, subprime lending, by making loans available to those who might not otherwise

* Professor of Law, Director for Curriculum and Public Service, Justice Action Center, New York Law School. Fordham, B.A. 1982; Harvard, J.D. 1985. Served in Civil Division of Legal Aid Society. Authority on lending and banking law with specialty in Community Reinvestment and Home Mortgage Disclosure legislation.

qualify for a loan, may help a bank satisfy the demand for loans. On the other hand, subprime loans may be crowding out prime loans, leaving the prime segment of the market in low- and moderate-income communities without access to prime loans.

This paper examines the relationship between predatory lending, subprime lending, and the CRA obligations of banks to meet the credit needs of their communities in a safe and sound manner. Section I of the paper presents a summary of the CRA law and regulations, focusing on those provisions that relate to lending. Section II of this paper examines specific regulations and regulatory statements that address the relationship between predatory lending, subprime lending, and the CRA. Specifically, Section II addresses whether predatory lending and subprime lending help address the credit needs of the community, whether they are consistent with safe and sound lending practices, and whether they constitute illegal or discriminatory credit practices. Section II concludes that predatory lending does not meet the credit needs of the community, is not safe and sound, and is an illegal credit practice. A bank engaged in predatory lending is thus not meeting its CRA obligations and should be penalized with a reduced CRA rating. Subprime lending is not as clear: it may help meet credit needs; it may be safe and sound; and it may constitute an illegal or discriminatory lending practice. A bank that is engaged in subprime lending should thus be subject to increased CRA scrutiny, and Section II sketches a brief description of the form this scrutiny might take. Finally, Section II addresses proposals to increase the information disclosures lenders must make to assist efforts to detect predatory and subprime lending.

I. BACKGROUND—CRA LAW AND REGULATIONS

A. *The Community Reinvestment Act*

The Community Reinvestment Act¹ (“CRA”) is a relatively brief federal law that states that “banks have a continuing and affirmative obligation to help meet the credit needs of the local communities in which they are chartered.”² The purpose of the CRA is to require the federal banking regulatory agencies “to encourage such institutions to help meet the credit needs of the local communities in which they are

1. 12 U.S.C.A. §§ 2901-2908 (1989 & Supp. 2000).

2. 12 U.S.C.A. § 2901(a)(3).

chartered consistent with the safe and sound operation of such institutions.”³

Four federal banking regulatory agencies are responsible for enforcing the CRA: the Comptroller of the Currency for national banks; the Board of Governors of the Federal Reserve System for state-chartered banks that are members of the Federal Reserve System; the Federal Deposit Insurance Corporation for state-chartered banks that are not members of the Federal Reserve System; and the Office of Thrift Supervision for savings associations.⁴ The CRA directs each agency to assess the performance of each bank it supervises at “meeting the credit needs of its entire community, including low- and moderate-income neighborhoods, consistent with the safe and sound operation of such institution”⁵ The CRA also directs each agency to “take such record into account in its evaluation of an application for a deposit facility by such institution.”⁶ An application for a deposit facility includes six different types of applications: an application to the appropriate federal banking regulatory agency for a national bank charter; deposit insurance; the establishment of a branch; the relocation of a branch or home office; the merger or consolidation with, or the acquisition of the assets, or the assumption of the liabilities of a bank; or the acquisition of shares in, or the assets of, a bank.⁷

After completing its assessment of a bank’s record at meeting the credit needs of its entire community, including low- and moderate-income neighborhoods, the relevant federal banking regulatory agency is to prepare a written evaluation report.⁸ The public section of the report is to state the agency’s conclusion for each CRA performance factor in the CRA regulations, the facts and data supporting these conclusions, and the bank’s CRA rating with an explanation for the rating.⁹ There are four possible CRA performance ratings: outstanding; satisfactory; needs to improve; and substantial noncompliance.¹⁰ For a bank with an office in more than one metropolitan area, the federal banking agency is to assess its performance in each metropolitan area separately, but does not give a separate CRA performance rating for

3. *Id.* at § 2901(b).

4. *See id.* at § 2902(1).

5. *Id.* at § 2903(a)(1).

6. *Id.* at § 2903(a)(2).

7. *See id.* at § 2902(3).

8. *See* 12 U.S.C.A. § 2906(a)(1).

9. *See id.* at § 2906(b)(1)(A).

10. *Id.* at § 2906(b)(2).

each metropolitan area.¹¹ For a bank with an office in more than one state, the federal banking regulatory agency is to provide an evaluation of the bank's record in each state separately.¹²

B. The CRA Regulations

The CRA requires the federal banking agencies to promulgate regulations enforcing the CRA.¹³ They have promulgated substantially identical regulations.¹⁴ The regulations include several provisions particularly relevant to issues relating to predatory and subprime lending. These include the rules for delineating a CRA assessment area, the criteria for evaluating the CRA record of banks of different sizes and types, the rules for assigning a CRA rating to a bank, and the effect that discriminatory or other illegal credit practices have on a bank's CRA rating.

1. The CRA Assessment Area

The regulations require each bank to delineate one or more "assessment" areas in which its performance at meeting the credit needs of its community will be evaluated.¹⁵ This assessment area must consist of one or more metropolitan statistical areas or contiguous political subdivisions and should include those census tracts in which the bank has its home office, branches, deposit-taking ATMs, and the surrounding census tracts in which the bank has made a substantial portion of its loans.¹⁶

2. The "Large Bank" CRA Performance Test

"Large" banks with \$250 million or more in assets are evaluated for CRA performance according to the lending, investment, and service tests.¹⁷ Under the lending test, the agency considers the bank's loan originations and purchases and, at the bank's option, the lending

11. *Id.* at § 2906(b)(1)(B).

12. *Id.* at § 2906(d)(1)(A).

13. *See id.* at § 2905.

14. The agencies' regulations are promulgated in the following places: Comptroller of the Currency—12 C.F.R. pt. 25 (2001); Federal Reserve—12 C.F.R. pt. 228 (2001); Federal Deposit Insurance Corporation—12 C.F.R. pt. 345 (2001); Office of Thrift Supervision—12 C.F.R. pt. 563e (2001). (The following description of the CRA regulations includes citations only to the Comptroller of the Currency's regulations.)

15. 12 C.F.R. § 25.41(a).

16. *Id.* at § 25.41(c).

17. *Id.* at § 25.21.

originations and purchases of its affiliates.¹⁸ The agencies consider five performance criteria under the lending test: the total number and dollar amount of the bank's home mortgage, small business, small farm, and, in certain cases, consumer loans; the geographic distribution of the bank's loans, including the proportion of the bank's lending in its assessment area, the dispersion of lending in the bank's assessment area, and the number and dollar amount of loans in low-, moderate-, middle-, and upper-income areas; the distribution of the bank's loans according to the income of the borrower; the bank's community development lending, including the number and dollar amount of community development loans and their innovativeness and complexity; and the bank's use of innovative or flexible lending practices in a safe and sound manner to address the credit needs of low- and moderate-income borrowers or neighborhoods.¹⁹ Under the investment test, the agency evaluates the bank's community development investments according to the following criteria: total dollar amount of the investments; innovativeness or complexity of the investments; responsiveness of the investments to credit and community development needs; and the degree to which the qualified investments are not routinely provided by private investors.²⁰ Under the service test, the agency evaluates the bank's retail banking services and community development banking services, including the distribution of the bank's branches among low-, moderate-, middle-, and upper-income neighborhoods; the bank's record of opening and closing branches in low- and moderate-income neighborhoods; and the availability of alternative means to deliver banking services to low- and moderate-income persons and neighborhoods.²¹

The agency assigns a rating to the bank's performance on each of these three tests, and then combines them for a final CRA rating.²² In the final CRA rating, the rating on the lending test counts for at least twice as much as the rating on either the lending or the investment tests.²³

18. *See id.* at § 25.22(a)(1) and (c)(1).

19. *Id.* at § 25.22(b).

20. *Id.* at § 25.23(e).

21. 12 C.F.R. § 25.24(d).

22. *See id.* at §§ 25.22(e), 25.23(f), 25.24(f), 25.28, and 12 C.F.R. pt. 25, app. A.

23. 60 Fed. Reg. 22,156, 22,168-22,170 (July 1, 1995) (to be codified at 12 C.F.R. pts. 25, 228, 345, 563e, 203).

3. *The "Small Bank" CRA Performance Test*

"Small" banks with less than \$250 million in assets²⁴ are evaluated for CRA performance according to five criteria: the bank's loan-to-deposit ratio; the percentage of loans in the bank's assessment area; the bank's record of lending to borrowers of different income levels; the geographic distribution of the bank's loans; and the bank's record of taking action in response to written complaints about its performance in helping to meet credit needs in its assessment area.²⁵ A small bank is eligible for a satisfactory CRA rating if its loan-to-deposit ratio is reasonable, a majority of loans are in its service area, its distribution of loans among individuals and neighborhoods of different income levels is reasonable, and it is generally responsive to complaints from the community.²⁶ A small bank is eligible for an outstanding rating if it meets all of these standards and exceeds some, and will receive a needs-to-improve or substantial noncompliance rating depending on the degree to which it has failed to meet these standards.²⁷

4. *The "Wholesale and Limited Purpose Bank" CRA Performance Test*

A wholesale bank that generally does not provide credit to the general public²⁸ or a limited purpose bank that provides only a narrow product line²⁹ is evaluated for CRA compliance according to its total number and dollar amount of community development loans, investments, and services; the use of innovative or complex qualified investments, loans, or services and the extent to which they are not provided by others; and the bank's responsiveness to credit and community development needs.³⁰

5. *Effect of Discriminatory or Other Illegal Credit Practices*

Evidence that a bank has engaged in discriminatory or other illegal credit practices will adversely affect a bank's CRA rating, whether the bank be a large bank, small bank, or wholesale or limited purpose bank.³¹ In determining the effect such evidence will have, the relevant

24. 12 C.F.R. § 25.12(t).

25. *Id.* at § 25.26(a).

26. 12 C.F.R. pt. 25 app. A § (d)(1).

27. *Id.* at §§ (d)(1) and (d)(2).

28. 12 C.F.R. § 25.12(w).

29. *Id.* at § 25.12(o).

30. *Id.* at § 25.25(c).

31. *Id.* at § 25.28(c).

2002-2003]

COMMUNITY REINVESTMENT ACT

741

agency will take into account the nature and extent of the evidence, the policies and procedures the bank has in place to prevent discriminatory or other illegal credit practices, and any corrective action the bank has taken.³²

II. SUBPRIME AND PREDATORY LENDING AND A BANK'S CRA OBLIGATIONS

This Section examines the relationship between subprime lending, predatory lending, and a bank's CRA obligations. Section II. A. describes the federal banking agencies' definition of predatory and subprime lending. Section II. B. to II. D. then examines the relationship between the CRA and predatory and subprime lending by investigating whether predatory and subprime lending help meet the credit needs of the community, whether they are safe and sound lending practices, and whether they constitute illegal or discriminatory lending practices. Finally, Section II. E. describes proposals to expand the ability of the federal banking agencies to detect subprime and predatory lending practices.

A. *Definitions of Subprime and Predatory Lending*

The federal banking agencies have issued definitions of both subprime and predatory lending in a joint policy statement on subprime lending.³³ According to the federal banking agencies, a subprime loan is one made to a borrower with a weak credit history or repayment capacity.³⁴ A subprime borrower will generally have one or more of the following characteristics: two or more 30-day delinquencies in the last year or one or more 60-day delinquencies in the last two years; judgment, foreclosure, repossession or charge-off in the prior 24 months; bankruptcy in the last five years; relatively high default probability as evidenced by a FICO score of 660 or below; or a debt service-to-income ratio of 50 percent or greater.³⁵

The federal banking agencies define predatory lending as a subset of subprime lending that is "abusive or predatory."³⁶ They state that

32. *Id.*

33. BOARD OF GOVERNORS OF THE FEDERAL RESERVE SYSTEM, FEDERAL DEPOSIT INSURANCE CORPORATION, OFFICE OF THE COMPTROLLER OF THE CURRENCY & OFFICE OF THRIFT SUPERVISION, EXPANDED GUIDANCE FOR SUBPRIME LENDING PROGRAMS (2001).

34. *Id.* at 2.

35. *Id.* at 2-3.

36. *Id.* at 10.

predatory loans “appear to be designed to transfer wealth from the borrower to the lender/loan originator without a commensurate exchange of value.”³⁷ Predatory lending practices generally include at least one of the following three characteristics: making unaffordable loans based on the assets of the borrower rather than on the borrower’s ability to repay; inducing a borrower to refinance a loan repeatedly in order to charge high points and fees each time the loan is refinanced; or engaging in fraud or deception to conceal the true nature of the loan obligation from an unsuspecting or unsophisticated borrower.³⁸

B. Meeting the Credit Needs of the Community

As described in Section I, the purpose of the CRA is to encourage banks to “meet the credit needs” of their local communities, including low- and moderate-income neighborhoods. Meeting the credit needs of the community has at least two components: originating a sufficient number of loans in the community so that the demand for loans is met and originating loans that “meet” the credit needs of the borrower in that they are on the best possible terms for and affordable to the borrower. By defining predatory lending the way they have, the federal banking agencies have made fairly clear that a predatory loan does not “meet” credit needs and thus does not help a bank satisfy its CRA obligations. The relationship between subprime lending and meeting the credit needs of the community is more complex and is evolving. A bank that is engaged in subprime lending, which by definition is more costly to the borrower than prime lending, may be failing to “meet” the credit needs of the community; while it may be originating a large number of loans, these loans may not be on the best terms for and affordable to the borrower. A bank engaged in subprime lending may be missing the opportunity to meet the demand for prime loans in its community, sweeping prime borrowers into its subprime lending program, or failing to devise other innovative loan programs that could make loans to subprime borrowers at lower interest rates. This all would be inconsistent with a bank’s CRA obligations. The federal banking agencies have not yet reconciled subprime lending with the CRA’s purpose, but they are thinking about how to do so.

37. *Id.*

38. *Id.* at 10-11.

The federal banking agencies recently issued an Advance Notice of Proposed Rulemaking Regarding the Community Reinvestment Act.³⁹ In the Notice, they seek public input about potential changes to the CRA regulations. One of the points the agencies raise involves subprime and predatory lending. Specifically, the agencies state, “some are concerned that the regulations generally seem to provide consideration of loans without regard to whether the lending activities are appropriate.”⁴⁰ The agencies state that persons concerned about this suggest that “a CRA examination also should include consideration of whether certain loans contain harmful or abusive terms and, therefore, do not help meet community credit needs.”⁴¹ The agencies then ask, “Does the lending test effectively assess an institution’s record of helping to meet the credit needs of its entire community? Is so, why? If not, how should the regulations be revised?”⁴² A general answer to these questions is that the federal banking agencies already have the tools available to regulate predatory and subprime lending for CRA purposes, but explicit guidance would be helpful.

As far as predatory lending is concerned, the answer to the agencies’ question seems clear. Predatory lending, as defined by the federal banking agencies, does not help meet credit needs and thus does not help a bank meet its CRA obligations. Despite the fact that the federal banking agencies already have the tools available to regulate predatory lending for CRA purposes, explicit guidance in the CRA regulations would be helpful.

The answer to the agencies’ question is somewhat more complicated regarding subprime lending. Subprime lending is a legitimate business practice and likely makes loans available to low- and moderate-income persons who would not otherwise be eligible for a loan. Thus, unlike predatory lending, subprime lending can help meet the credit needs of the community. On the other hand, subprime lenders may be failing to meet the demand for prime loans and may be missing opportunities to create innovative loan programs; and thus may not be helping to meet the credit needs of the community.

Currently, several provisions of the CRA regulations would allow the federal banking agencies to take into account a bank’s subprime

39. Community Reinvestment Act Regulations, 66 Fed. Reg. 37,602 (reviewed July 19, 2001) (to be codified at 12 C.F.R. pts. 228, 345, 563e, 25).

40. *Id.* at 37,604.

41. *Id.*

42. *Id.*

lending record in evaluating its CRA record. The CRA regulations, like the statute, require banks to “help meet the credit needs” of their local communities.⁴³ This provision can be read to authorize the federal banking agencies to investigate during a CRA examination whether a subprime lender is missing opportunities to make prime or less expensive loans in its community. Additionally, one provision of the lending test for large banks requires the federal banking agencies to evaluate the bank’s use of flexible or innovative lending practices to help meet the credit needs of low- and moderate-income borrowers or neighborhoods.⁴⁴ The federal banking agencies could use this criterion to evaluate whether a bank could be providing subprime borrowers with different, more innovative loan products that are less expensive.

Despite these provisions, direct guidance in the CRA regulations about subprime lending and the CRA obligations of banks would certainly be helpful. The starting point for such guidance should be that a bank’s subprime lending will be evaluated within the context of the bank’s overall lending and the credit needs of the community. Relevant criteria would include the percentage of the bank’s loans in low- and moderate-income neighborhoods that are subprime, the bank’s market share of all home mortgage loans in low- and moderate-income neighborhoods, and the records of peer banks on comparable criteria. For example, imagine 90% of one bank’s home mortgage loan originations in low- and moderate-income neighborhoods are subprime and the bank’s market share of all home mortgage loans in low- and moderate-income neighborhoods is 2%. Imagine now 10% of a peer bank’s home mortgage loan originations in low- and moderate-income neighborhoods are subprime and its market share of home mortgage loans in low- and moderate-income neighborhoods is also 2%. The second bank appears to be doing a better job at meeting the credit needs of low- and moderate-income neighborhoods because it is making the same number of loans as the first bank but relatively fewer subprime loans. When the federal banking agencies examine the CRA record of the first bank, they should take this into account, and examine whether the first bank is failing to meet its CRA obligations by, for example, failing to engage in innovative lending programs or by targeting low- and moderate-income neighborhoods for subprime loans without meeting the need for prime lending in those neighborhoods.

43. *See id.* at §§ 25.21(c), 25.22(a) (2002).

44. 12 C.F.R. § 25.22(b)(5).

2002-2003]

COMMUNITY REINVESTMENT ACT

745

C. Safe and Sound Lending Practices

As described in Section I, central to a bank's CRA obligation to help meet the credit needs of its local community is that the bank must do so in a safe and sound manner. If a loan is not safe and sound, the loan cannot count toward satisfying the bank's obligation to meet the credit needs of its local community.⁴⁵ In the *Guidance for Subprime Lending Programs*, the federal banking agencies offered guidance about the relationship between subprime lending, predatory lending, safe and sound banking practices, and the CRA.

The *Guidance* states that banks that have subprime lending programs with an aggregate credit exposure greater than or equal to 25 percent of tier one capital are subject to additional regulatory scrutiny for safe and sound lending practices.⁴⁶ The *Guidance* provides that such banks should have special procedures in place to manage the additional risks associated with subprime lending, should set aside in their loan loss allowance an amount that is sufficient to cover all estimated losses from subprime lending during a twelve month period, and should hold capital against subprime loan portfolios in an amount that is one-half to three times greater than what is appropriate for non-subprime assets of a similar type.⁴⁷ A bank with a subprime lending program that does not satisfy these requirements is engaging in unsafe and unsound banking practices, and such loans cannot count towards satisfying the bank's CRA obligations.

The *Guidance* states that predatory loans are unsafe and unsound loans. "Loans to borrowers who do not demonstrate the capacity to repay the loan, as structured, from sources other than the collateral pledged are generally considered unsafe and unsound."⁴⁸ As such, predatory loans do not count toward satisfying a bank's CRA obligations.

D. Discriminatory and Other Illegal Credit Practices

The CRA regulations currently state that evidence of discriminatory or other illegal credit practices will affect a bank's CRA rating. In two separate regulatory statements, the federal banking agencies have addressed the relationship between illegal credit practices and preda-

45. *See id.* at § 25.21(d).

46. GUIDANCE FOR SUBPRIME LENDING PROGRAMS, *supra* note 33, at 2.

47. *Id.* at 3-6.

48. *Id.* at 11.

tory lending. However, the two statements appear to be somewhat inconsistent and need to be reconciled. In addition, the agencies have not explicitly addressed the relationship between predatory and subprime lending and discriminatory lending practices.

The first regulatory statement appears in a recent addition to the Interagency Questions and Answers Regarding the Community Reinvestment Act (the "CRA Q & A").⁴⁹ In response to the hypothetical question—"What is meant by discriminatory or other illegal credit practices?"—posed in the CRA Q & A, the agencies have added the following provision intended to show that predatory lending will have a negative effect on a bank's CRA rating:

Examples of other illegal credit practices inconsistent with helping to meet community credit needs include violations of:

The Truth in Lending Act regarding rescission of certain mortgage transactions and regarding disclosures and certain loan term restrictions in connection with credit transactions that are subject to the Home Ownership and Equity Protection Act;

The Real Estate Settlement Procedures Act regarding the giving and accepting of referral fees, unearned fees or kickbacks in connection with certain mortgage transactions; and

The Federal Trade Commission Act regarding unfair or deceptive acts or practices.⁵⁰

This addition to the CRA Q & A thus provides that violations of the Truth in Lending Act ("TILA") in connection with loans protected by the Home Ownership Equity Protection Act ("HOEPA"), the Real Estate Settlement Procedures Act ("RESPA"), and the Federal Trade Commission Act ("FTCA") may result in a reduced CRA rating.

The CRA Q & A's definition of a predatory loan—a loan that violates TILA, RESPA, or the FTCA—is not as broad as the agencies' definition of predatory or abusive lending in another regulatory statement, the federal banking agencies' *Guidance on Subprime Lending*.⁵¹ The definition of predatory lending in the *Guidance* includes "unaffordable

49. Community Reinvestment Act: Interagency Questions and Answers Regarding Community Reinvestment, 66 Fed. Reg. 36,620 (amended and republished July 11, 2001).

50. *Id.* at 36, 640.

51. See EXPANDED GUIDANCE FOR SUBPRIME LENDING PROGRAMS, *supra* note 33.

loans based on the assets of the borrower rather than on the borrower's ability to repay an obligation."⁵² In the *Guidance*, the federal banking agencies indicate that predatory loans are unsafe and unsound, should be criticized in the bank's Report of Examination as imprudent, and should be referred to the relevant agency's consumer compliance and fair lending specialists for further review.⁵³ Predatory lending, as unsafe and unsound, at the very least constitutes evidence of illegal lending practices, thus subjecting the bank to a lower CRA rating.

The federal banking agencies have not issued guidance about the relationship between discriminatory credit practices and subprime and predatory lending. There are potentially at least three practices involving predatory and subprime lending that may be discriminatory. The first is targeting minority individuals or predominantly minority communities for subprime or predatory loans, resulting in a disproportionate number of loans on less advantageous terms to these borrowers and neighborhoods than to white borrowers or predominantly white neighborhoods. The second is failing to refer prime minority borrowers who apply for subprime loans to more favorable prime loans while referring similarly situated white borrowers to prime loans. The third is offering mortgage officers and brokers higher commissions for making loans with higher rates, creating an incentive for officers and brokers to take advantage of minority loan applicants by offering them higher-priced loans. Agency guidance on the relationship between such practices and discriminatory lending practices would be very helpful.

E. Detecting Subprime and Predatory Lending: Affiliates, Assessment Areas, and Data

Several provisions of the CRA regulations as described in Section I make it difficult to evaluate the full extent of a bank's subprime or predatory lending. First, the lending records of a bank's affiliates are included in the bank's CRA evaluation only at the bank's option. In order for a bank to escape CRA scrutiny of its subprime or predatory lending while allowing the parent company to reap all the profits of subprime and predatory lending, a bank could make sure that it engages in prime lending only, leaving subprime or predatory lending to its affiliates and not including its affiliates' lending in the bank's CRA

52. *Id.* at 10.

53. *Id.* at 11.

examination.⁵⁴ Second, a bank is assessed for CRA compliance only in the metropolitan areas in which it has a branch or home office, and within those metropolitan areas it is only evaluated for CRA compliance only in its self-described assessment area. This means that potentially, only a small proportion of a large bank's lending may come under CRA scrutiny, allowing subprime or predatory lending outside these areas to escape CRA-regulatory notice.⁵⁵ Finally, the CRA does not contain any provisions requiring lenders to disclose data about subprime lending. The Home Mortgage Disclosure Act ("HMDA") requires lenders to disclose information about their home mortgage loans.⁵⁶ The Federal Reserve recently adopted new HMDA regulations designed to help the federal banking agencies identify subprime and predatory lending.⁵⁷ The new regulations, which will become effective for loans made in 2004, require lenders to disclose whether a loan is covered by HOEPA and to disclose the difference between the interest rate on the loan and the yield on Treasury securities of similar duration.

CONCLUSION

The relationship between predatory lending, subprime lending, and a bank's CRA obligations is evolving. Predatory lending does not help a bank satisfy its obligations to meet the credit needs of its community, is not a safe and sound banking practice, and is evidence of illegal credit practices, subjecting a bank to a reduced CRA rating. Subprime lending can help a bank meet the credit needs of its community, but the federal banking agencies must carefully scrutinize it when evaluating the CRA record of a bank to ensure that the bank's subprime lending is not replacing prime lending, is done in a safe and sound way, and is not discriminatory.

54. See National Community Reinvestment Coalition, *Comments on Advance Notice of Proposed Rulemaking Regarding the Community Reinvestment Act 5*, Oct. 2, 2001 (on file with the New York Law School Journal of Human Rights).

55. See NATIONAL COMMUNITY REINVESTMENT COALITION, ANTI-PREDATORY LENDING TOOLKIT 28 (2d ed. 2002), available at http://www.ncrc.org/svcs/Toolkit_w_covers.pdf (last visited Aug. 22, 2002).

56. 12 U.S.C. §§ 2801-2810 (1989 & Supp. 2000).

57. Home Mortgage Disclosure, 67 Fed. Reg. 7222 (Feb. 15, 2002) (to be codified at 12 C.F.R. pt. 203).