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## Introduction

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RICHARD MARSICO

## Introduction

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This symposium issue of the *New York Law School Law Review* is devoted to the thirtieth anniversary of Community Reinvestment Act (“CRA”).<sup>1</sup> The key question about the CRA as it enters its fourth decade is whether it is still relevant, let alone whether it will continue to be relevant for another thirty years. In answering this question, it is helpful to identify the CRA’s goals, the means for achieving these goals, and its justifications.

Congress’ goals in passing the CRA were to eliminate the related practices of bank redlining and capital export.<sup>2</sup> Local bank branches would take deposits from local neighborhood residents, and instead of returning the deposits to the residents in the form of home mortgage or other loans would “redline” the local neighborhoods and refuse to make loans there. The banks would then export this deposit capital to other communities, leaving their local neighborhoods starved for investment capital. Redlining and capital export caused or contributed to a cycle of disinvestment in and decline of urban, lower-income, and predominantly minority neighborhoods. Congress hoped that the CRA would help end these related practices and revitalize these underserved neighborhoods.

The means Congress employed for ending redlining and capital export were straightforward. The CRA was and is a relatively simple law.<sup>3</sup> It places on banks an ongoing and affirmative obligation to “meet the credit needs of the local communities in which they are chartered,” including low- and moderate-income (“LMI”) neighborhoods.<sup>4</sup> It requires the four federal agencies that regulate banks to evaluate the record of each regulated bank at meeting local credit needs, to issue periodic written CRA performance evaluation reports that include a CRA rating, and to take account of a bank’s record of meeting community credit needs when deciding whether to grant its expansion applications.<sup>5</sup> The agency can approve, deny, or delay a merger based on the bank’s CRA record.<sup>6</sup>

There were three main justifications for the CRA. The first was that banks were chartered to meet the convenience and needs of their communities, which includes meeting the credit needs of their communities. The second justification took the form of a quid pro quo. Banks received from the government significant advantages over their competitors, including a quasi-monopoly, relatively inexpensive deposit insurance, and exclusive access to cheaper money. In return, it was fair to ask them to meet the public purpose of satisfying local credit needs. The final justification

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1. 12 U.S.C. §§ 2901–2908 (2006).

2. See John Taylor & Josh Silver, *The Community Reinvestment Act at 30: Looking Back and Looking to the Future*, 53 N.Y.L. SCH. L. REV. 203, 204 (2009); Warren Traiger, *The Community Reinvestment Act: A Welcome Anomaly in the Foreclosure Crisis*, 53 N.Y.L. SCH. L. REV. 227, 228–29 (2009).

3. See Traiger, *supra* note 2, at 229.

4. Taylor & Silver, *supra* note 2 (citing 12 U.S.C. § 2901 (2006)).

5. See Taylor & Silver, *supra* note 2, at 204–05. The federal banking agencies are the Board of Governors of the Federal Reserve System, the Office of the Comptroller of the Currency, the Federal Deposit Insurance Corporation, and the Office of Thrift Supervision. See *id.* For more information about these agencies and the banks they regulate, see Josh Silver & Richard Marsico, *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, 272 n.4 (2009).

6. See Taylor & Silver, *supra* note 2, at 206.

was fundamental fairness. It was only fair that banks, who were more than willing to take the deposits of local neighborhood residents and use them to make profits, should return those deposits in the form of loans to the community residents who supported the bank.

Thirty years after Congress passed the CRA, the market conditions underlying the CRA's goals, means, and justifications have changed. As to goals, although there is evidence that LMI communities and communities of color still receive a disproportionately low share of bank loans, these underserved communities are currently suffering more acutely from reverse redlining than traditional redlining, as lenders are targeting them for higher priced subprime loans, many of which contain predatory clauses that make repayment very difficult.<sup>7</sup> These loans are leading to record high rates of foreclosure with devastating consequences for borrowers and neighborhoods.<sup>8</sup> In addition, residents of underserved communities suffer from being on the wrong side of a two-tiered financial system, from which they lack access to bank branches and the cheaper deposit and loan products they offer, and instead are forced to deal with more expensive financial entities such as check cashers and payday lenders.<sup>9</sup> A law like the CRA that is designed to fight redlining and capital export is not necessarily well-suited to end reverse redlining or the two-tiered financial services system.

As to means, banks and the financial services industry have grown beyond the means the CRA employs to regulate them. Banks are no longer the dominant institutional provider of consumer financial services. Many financial services companies not covered by the CRA—including mortgage bankers, insurance companies, and securities dealers—provide a full array of deposit and credit products to consumers as well as other options for investing their money. In addition, banks are no longer the local, unitary institutions they were when the CRA was passed. They no longer simply take deposits from and make loans to local neighborhood residents through local bank branches. Instead, they are national and even international in scope. They are often one component part of multi-company holding companies and have affiliates and subsidiaries that perform traditional and non-traditional banking functions. The CRA, which covers only banks—defined narrowly as depository institutions—is not up to the task of regulating the entire financial services industry.

Finally, the CRA's justifications seem no longer fully applicable. The fundamental fairness argument appears to have gone the way of the neighborhood bank. Our highly mobile society and rapidly changing financial services industry does not create the image of a local bank taking deposits from local residents and lending the money back for home mortgages or other needs. The *quid pro quo* argument also has less support, as the quasi-monopoly, relatively low-cost deposit insurance, and access

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7. See Gregory D. Squires, *Urban Development and Unequal Access to Housing Finances Services*, 53 N.Y.L. Sch. L. Rev. 255, 259–63 (2009).

8. See *id.*

9. See *id.*

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to cheaper money that banks enjoy does not seem to give them the competitive advantage they once had. Finally, imposing a public purpose on banks stemming from their charter, while still a valid exercise of governmental power, seems unfair in light of the absence of such a requirement on banks' competitors, who did not really offer the competition to banks at the time Congress passed the CRA that they do now.

If the CRA's goals, means, and justifications are not as closely related to market reality as they were in 1977, the question is: What is to be done? Repeal the CRA? Allow it to fade into oblivion along with the neighborhood bank? Amend it to reflect current market conditions? One way to determine what is to be done with the CRA is to determine what the CRA has done. Broadly stated, the CRA has democratized capital.<sup>10</sup> It has done so in two ways. First, it has expanded the number of people who have a voice in how loan capital is distributed. This expansion is most obvious when community advocates oppose bank merger applications on the grounds that the bank has not met community credit needs. These so-called CRA challenges have led to trillions of dollars in community lending commitments by banks.<sup>11</sup> In addition, and not as obviously, members of the public exercise a say in the distribution of loan capital through the public CRA evaluation process, the threat of CRA challenges, and the public availability of significant amounts of important data about bank community lending records. The public nature of the CRA has put pressure on banks to work continuously to meet credit needs. The second way the CRA has democratized capital is that it has allowed more people to participate in the wealth-building possibilities of the economic system by influencing banks to make loans to buy a home or start a business. Several studies have documented the impact the CRA has had on lending and estimated that banks have made tens of thousands of loans they would not have made without the CRA.<sup>12</sup> As a result, the recipients of these loans are participating in the economic system in a way they would not have without the CRA.

The claim that the CRA has democratized capital can provide a framework for thinking about what is to be done with the CRA in the future. Continuing to give a voice to the community in lending decisions and continuing to expand the economic pie are the starting points. Two contemporary problems that should be addressed—reverse redlining and the two-tiered financial services system—demonstrate new aspects of democratizing capital. In *The Community Reinvestment Act at 30: Looking Backward and Looking to the Future*, John Taylor and Josh Silver present a comprehensive plan for developing the means for the CRA to accomplish its goal of democratizing capital.<sup>13</sup> The plan retains the basic requirement of the CRA—the ongoing obligation to meet the credit needs of local communities. It retains the public availability of data about bank lending and the public CRA evaluation pro-

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10. See RICHARD D. MARSICO, *DEMOCRATIZING CAPITAL: THE HISTORY, LAW, AND REFORM OF THE COMMUNITY REINVESTMENT ACT* (2005).

11. See Taylor & Silver, *supra* note 2, at 206–09.

12. For a brief summary of these studies, see *id.*

13. For a brief summary of this plan, see *id.* at 224–25.

cess. The plan reflects the changes in the financial services industry and the changes in the character of banking from local to national to international since the CRA was passed, banks' loss of control over the consumer financial services market, and the growth of reverse redlining and the two-tiered financial system. Taylor and Silver's plan includes extending the CRA to cover financial services companies other than banks, expanding the geographic area in which banks have CRA obligations, requiring bank affiliates to be included in the bank's CRA evaluations, requiring CRA evaluations to evaluate lending based on race, and more rigorous evaluation of bank branching patterns.<sup>14</sup>

An article by Josh Silver and me and another by Warren Traiger support the proposition—crucial to the successful implementation of Taylor's and Silver's proposal—that the CRA has had a positive impact on bank lending decisions and that the criteria the federal banking agencies use in CRA performance evaluations influence bank lending practices.<sup>15</sup> In addition to Taylor's and Silver's suggestions for improving the CRA, Gregory Squires, in his article, *Uneven Development and Unequal Access to Housing Finance Services*, suggests that laws such as living wage laws that are designed to reduce the wealth and income gap are necessary before the two-tiered financial system or reverse redlining can be eliminated.<sup>16</sup>

Taylor and Silver first address both the fact that banks are no longer the dominant entity in the consumer financial services industry and the consequence that imposing community reinvestment obligations on banks alone cannot accomplish the goals of the CRA. They propose extending the CRA to cover the financial institutions that now compete with banks.<sup>17</sup> These entities include credit unions, mortgage banks, insurance companies, and securities firms. Silver and Taylor support this proposal by citing evidence that credit unions and mortgage companies do not perform as well as banks at serving the credit needs of local communities.<sup>18</sup> They also support the proposal by arguing that extending the CRA to insurance companies and securities firms would facilitate economic development and wealth-building among LMI and minority persons and communities.<sup>19</sup>

In his article, *The Community Reinvestment Act: A Welcome Anomaly in the Foreclosure Crisis*, Warren Traiger provides evidentiary support that expanding the coverage of the CRA to non-bank financial institutions might improve their sub-prime lending records, although Traiger himself does not make this proposal.<sup>20</sup> Traiger shows evidence that the CRA has an impact on bank lending behavior.<sup>21</sup>

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14. *See id.*

15. *See* Silver & Marsico, *supra* note 5, at 292; Traiger, *supra* note 2, at 229–30.

16. *See* Squires, *supra* note 7, at 265–66.

17. *See* Taylor & Silver, *supra* note 2, at 224–25.

18. *See id.* at 206–09.

19. *See id.*

20. *See* Traiger, *supra* note 2, at 228–29.

21. *See id.*

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Specifically, he finds that banks lending in the geographic areas in which they have CRA obligations made lower percentages of subprime loans than lenders not covered by the CRA.<sup>22</sup> Banks were two-thirds less likely to make subprime loans than non-bank lenders not covered by the CRA.<sup>23</sup> Although Traiger does not explicitly say so, a fair inference from his findings is that extending the CRA to non-bank financial institutions could improve their subprime lending records.

Second, Taylor and Silver address the fact that the CRA covers banks only in the geographic areas where they make loans and have branches. The growth of banks from local to national institutions that make loans not only in their local communities through local branches but nationally through several different distribution channels means that the CRA covers only a small part of their lending and makes it very difficult for the CRA to accomplish its goals.<sup>24</sup> To remedy this, Taylor and Silver propose expanding the area in which banks have CRA obligations from the communities in which they make loans and have branches to the communities in which they make a significant percentage of all the loans in those communities.<sup>25</sup>

Warren Traiger's article once again provides evidentiary support for this proposal, although Traiger again does not explicitly endorse it. Traiger's research shows that banks lending in the geographic areas in which they have CRA obligations were more likely to retain loans in their portfolio—a strong indicator that the loan is a safe and sound loan—than banks lending outside of the areas in which they have CRA obligations.<sup>26</sup> Once again, this finding suggests that expanding the geographical area in which banks have CRA obligations could help diminish subprime lending.<sup>27</sup>

Third, Taylor and Silver address the fact that banks are no longer unitary institutions but are frequently one part of a multi-layered financial holding company. Non-depository affiliates of banks that make loans are not covered by the CRA unless the bank elects that they be covered. This loophole allows a bank to make its CRA-related loans itself and take credit for them and to divert its non-CRA loans to its affiliates, thus artificially inflating its own CRA record.<sup>28</sup> The Joint Center for Housing Studies at Harvard University found that the failure to include affiliates in CRA exams, combined with limiting the geographic area in which banks have CRA

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22. *See id.*

23. *See id.*

24. *See* Taylor & Silver, *supra* note 2, at 209–10.

25. *See id.* at 210.

26. *See* Traiger, *supra* note 2, at 234–37.

27. *See, e.g.,* Taylor & Silver, *supra* note 2, at 209–10. During the 2008 presidential campaign, many commentators blamed the CRA for the subprime lending crisis. *See* Editorial, *Misplaced Blame*, N.Y. TIMES, Oct. 15, 2008, at A34. The Comptroller of the Currency denied this, citing evidence that lenders not regulated by the CRA made 75% of subprime loans. Remarks by John C. Dugan, Comptroller of the Currency, Before the Enterprise Network Conference, Nov. 18, 2008, *available at* <http://www.occ.gov/ftp/release/2008-136a.pdf>. The Federal Reserve made similar findings. *See* Robert B. Avery, Kenneth P. Brevoort & Glenn B. Canner, *The 2007 HMDA Data*, *available at* <http://www.federalreserve.gov/pubs/bulletin/2008/pdf/hmda07draft.pdf>.

28. *See* Taylor & Silver, *supra* note 2, at 211–12.

obligations, contributed to the fact that the CRA covered less than 30% of home mortgage loans in 2000.<sup>29</sup> To help remedy this, Taylor and Silver recommend that bank non-depository lending affiliates such as mortgage companies be included in the bank's CRA performance evaluation.<sup>30</sup>

Fourth, Taylor and Silver recognize that minority borrowers and neighborhoods receive a disproportionately low percentage of home mortgage loans and a disproportionately high share of subprime home mortgage loans. They point out that CRA performance evaluations do not consider a bank's lending by race and suggest that doing so might increase minority communities' and borrowers' shares of home mortgage loans and decrease their shares of subprime loans. They thus call on the federal banking agencies to consider a bank's lending by race when conducting bank CRA performance evaluations.<sup>31</sup>

Taylor and Silver address the growth of the two-tiered financial services system with proposals they make regarding the federal banking agencies' evaluation of bank branch locations. Taylor and Silver recognize the importance of access to bank branches and deposit accounts for LMI consumers. Banking relationships are important to LMI persons because the relationships allow them to accumulate savings for loan down payments and collateral requirements for home mortgage and small business loans.<sup>32</sup> Warren Traiger cites evidence showing a strong negative correlation between the number of bank branches in a neighborhood and the number of foreclosures in the neighborhood: as the number of branches goes up, the rate of foreclosure declines.<sup>33</sup> The federal banking regulatory agencies have traditionally not rigorously evaluated a bank's distribution of branch locations to determine whether they were serving LMI neighborhoods.<sup>34</sup> Additionally, following amendments to the CRA regulations in 2004 and 2005, the federal banking agencies reduced the amount of information banks had to provide about their branch locations in their CRA performance evaluations, making it more difficult, if not impossible, to evaluate the bank's branch distribution.<sup>35</sup> Silver and Taylor call on the federal banking agencies to develop "clear and objective measures" for evaluating the distribution of bank branches and whether the distribution adequately serves LMI neighborhoods.<sup>36</sup>

Several of Taylor's and Silver's proposals for improving the CRA share the underlying assumption that changing the way that the federal banking agencies evaluate bank CRA performance (e.g., expanding the geographic area in which banks have CRA obligations, including bank affiliate lending in CRA exams, considering

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29. *See id.*

30. *See id.* at 222–23.

31. *See id.* at 212–13.

32. *See id.* at 213.

33. *See id.* at 213–15.

34. *See id.*

35. *See* Silver & Marsico, *supra* note 5, at 292.

36. *See* Taylor & Silver, *supra* note 2, at 214.



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lending by race, and more rigorous evaluation of bank branch locations) will have an impact on bank lending. Josh Silver and I provide support for this assumption in *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*. Silver and I demonstrate that the CRA performance evaluations and the criteria the federal banking agencies employ affect bank behavior.<sup>37</sup> Silver and I examined the impact that the federal banking agencies' amendments to the CRA regulations in 2004 and 2005 had on bank community development lending. We found that changes that the Office of Thrift Supervision made to the CRA performance evaluations of large thrifts that decreased the importance of community development lending and investment led to decreases in community development and lending by large thrifts.<sup>38</sup> We also found that, when given the chance, large thrifts reduced the weight their community development lending and investment had on their CRA ratings when they had relatively poor records of community development lending and investment.<sup>39</sup>

Finally, in his article, *Uneven Development and Unequal Access to Housing Finance Services*, Gregory Squires looks beyond the CRA for solutions to the subprime and predatory lending crises and the emergence and growth of the two-tiered financial system.<sup>40</sup> Squires argues that the concentration of wealth and income at the top of the socioeconomic ladder combined with concentrations of poverty at the bottom have fueled subprime and predatory lending and the two-tiered financial system in underserved communities. While strengthening the CRA and related laws will help ameliorate these problems, they will not be sufficient; policies that address economic inequality must be instituted as well.

Squires cites several statistics that show the growing disparity between the upper and lower rungs of the economic ladder. For example, “[b]etween 1967 and 2005, the share of income in the U.S. going to the top quintile of all households increased from 43.6% to 50.4%, while the share going to the bottom fifth dropped from 4.0% to 3.4%.<sup>41</sup> Between 1983 and 2001, the share of wealth held by the top 5% grew from 56.1% to 59.2%.<sup>42</sup> The consequences of this uneven development, according to Squires, include the two-tiered financial services system and the disproportionate growth of subprime and predatory lending in underserved neighborhoods.<sup>43</sup>

Squires recommends several proposals to address the underlying inequality, including indexing the federal minimum wage to inflation, adopting living wage laws, expanding the Earned Income Tax Credit, inclusionary zoning laws, and tax-based

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37. See Silver & Marsico, *supra* note 5, at 284–85.

38. See *id.* at 279–82.

39. See *id.*

40. See Squires, *supra* note 7, at 256–58.

41. *Id.* at 257.

42. *Id.* at 258.

43. See *id.* at 260–64.

revenue sharing.<sup>44</sup> He also recommends laws and policies addressed directly to the financial services industry, including expanding incentives for banks to provide electronic banking, CRA sanctions for banks that engage in predatory lending and credit for those that pursue equitable lending, expanding the CRA to cover a range of non-bank lenders, passing a strong anti-predatory lending law, more aggressive enforcement of the fair-lending laws, and imposing a loan suitability requirement on lenders.<sup>45</sup>

As the CRA hits early middle age, it is at a crossroads. It can continue on its current path, which will likely lead it to oblivion. Or it can modernize and rise to the challenge of regulating the financial services industry that has grown around it. The articles in this issue suggest how the CRA should be improved and describe other laws that should be passed to help the CRA to continue to democratize capital. It is up to Congress and the federal banking agencies to take up the challenge and improve the CRA.

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44. *See id.* at 265–66.

45. *See id.* at 265–68.