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Urban Development and Unequal Access to Housing Finance Services

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Urban Development and Unequal Access to Housing Finance Services

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Dramatic changes have taken place in the nation's mortgage lending markets in recent years. Passage of the Community Reinvestment Act ("CRA") in 1977, enforcement of the federal Fair Housing Act ("FHA"), and compliance with a range of local, state, and national fair lending rules have increased access to credit for many households and communities long denied conventional financial services. But within the past decade the rise in subprime and predatory lending has put many families and neighborhoods in financial jeopardy as default and foreclosure rates are skyrocketing, particularly in minority and low income areas. Fingers are pointed in several directions: greed on the part of families trying to buy homes they could not afford, lax underwriting by originators, inaccurate appraisals, fraudulent practices by investment bankers, inattention by regulators, and more. Community groups, elected officials, bank regulators, and mortgage lenders themselves are debating over how the nation should respond.

Lost amidst recent debates is the central role that surging economic inequality has played. The concentration of income and wealth at the top coupled with the concentration of poverty have nurtured significant increases in subprime and predatory lending among vulnerable communities. Strengthening the CRA and enforcing its provisions are necessary but not sufficient conditions for ameliorating the crises created by recent lending practices. Broader, macro-economic policies that directly address various trajectories of economic inequality must complement progressive banking and bank regulatory reforms if emerging challenges are to be met. This article examines the impact of inequality on subprime and predatory lending and offers a range of policy responses to the emerging problems confronting urban communities across the country.

The following section documents the growing polarization in the distribution of income and wealth. The consequences of such patterns are explored in the subsequent section. This is followed by a review of the impact of uneven development on financial services. The article concludes with a discussion of the public policies and private practices that created the uneven development and proposes alternatives that can ameliorate that inequality along with many of the ensuing social costs.

Surging Inequality

By virtually any measure economic inequality has increased in recent decades. Between 1967 and 2007, the share of income in the U.S. going to the top quintile of all households increased from 43.6% to 49.7%, while the share going to the bottom fifth dropped from 4.0% to 3.4%.¹ Since the mid 1970s, compensation for the 100 highest paid chief executive officers increased from \$1.3 million, or thirty-nine times the pay of the average worker, to \$37.5 million, or more than 1,000 times the pay of a typical worker.² In 2004, those in the top one percent enjoyed a 12.5% increase in their incomes compared to 1.5% for the remaining 99%.³

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1. CARMEN DENAVAS-WALT, BERNADETTE D. PROCTOR & JESSICA C. SMITH, U.S. CENSUS BUREAU, *INCOME, POVERTY, AND HEALTH INSURANCE COVERAGE IN THE UNITED STATES: 2007* 40 (2008).
 2. Paul Krugman, *For Richer*, N.Y. TIMES MAG., Oct. 20, 2002, at 62.
 3. Paul Krugman, Editorial, *Left Behind Economics*, N.Y. TIMES, July 14, 2006, at A19.

Wealth, of course, has long been much more unequally distributed than income, and that inequality has increased over time. Between 1983 and 2001, the share of wealth going to the top five percent grew from 56.1% to 59.2%. While African Americans and Hispanics earn approximately two-thirds of what whites earn, wealth holdings for the typical non-white family are approximately one-tenth that of the typical white family.⁴

City residents have been falling behind their suburban counterparts, and non-white neighborhoods have been falling behind white communities. In 1960, per capita income in cities was 105% that of suburbanites, but by 1990, urban residents were earning just 84% of those in the suburbs.⁵ The median census tract income for the typical black household in 1990 was \$27,808 compared to \$45,486 for whites, a gap of \$17,679. A similar pattern holds for Hispanics.⁶

Between 1970 and 2000, the number of high poverty census tracts (those where 40% or more of the population is poor) grew from 1177 to 2510, and the number of people living in those tracts grew from 4.1 million to 7.9 million.⁷ The isolation of rich and poor families is also reflected by the declining number of middle-income communities.⁸ Between 1970 and 2000, the number of middle income neighborhoods (census tracts where the median family income is between 80% and 120% of the median family income for the metropolitan area) dropped from 58% to 41% of all metropolitan area neighborhoods.⁹ And whereas more than half of lower-income families lived in middle income neighborhoods in 1970, only 37% of such families did so in 2000.¹⁰ The share of low-income families in low-income areas grew from 36% to 48%.¹¹

Even longer standing patterns of racial segregation persist. Nationwide, the black/white index of dissimilarity declined from .73 to .64 between 1980 and 2000.¹²

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4. THOMAS M. SHAPIRO, *THE HIDDEN COST OF BEING AFRICAN AMERICAN* 48–49 (2006); *see also* NAT'L CMTY. REINVESTMENT COAL. & WOODSTOCK INST., *A LIFETIME OF ASSETS* (2006).
 5. *INTERWOVEN DESTINIES: CITIES AND THE NATION* 25 (Henry G. Cisneros ed., 1993); JOHN R. LOGAN, LEWIS MUMFORD CTR. FOR COMPARATIVE URBAN AND REGIONAL RESEARCH, UNIV. AT ALBANY, *THE SUBURBAN ADVANTAGE: NEW CENSUS DATA SHOW UNYIELDING CITY-SUBURB ECONOMIC GAP, AND SURPRISING SHIFTS IN SOME PLACES* (2002).
 6. JOHN R. LOGAN, LEWIS MUMFORD CTR. FOR COMPARATIVE URBAN REGIONAL RESEARCH, UNIV. AT ALBANY, *SEPARATE AND UNEQUAL: THE NEIGHBORHOOD GAP FOR BLACKS AND HISPANICS IN METROPOLITAN AMERICA* tbl. 1 (2002).
 7. *Compare* PAUL A. JARGOWSKY, *POVERTY AND PLACE: GHETTOS, BARRIOS, AND THE AMERICAN CITY* 34 (1998) (reporting 1970 figures), *with* PAUL A. JARGOWSKY, BROOKINGS INST., *STUNNING PROGRESS, HIDDEN PROBLEMS: THE DRAMATIC DECLINE OF CONCENTRATED POVERTY IN THE 1990s* 20 (2003).
 8. JASON C. BOOZA, JACKIE CUTSINGER & GEORGE GALSTER, BROOKINGS INST., *WHERE DID THEY GO? THE DECLINE OF MIDDLE-INCOME NEIGHBORHOODS IN METROPOLITAN AMERICA* 1 (2006).
 9. *Id.*
 10. *Id.*
 11. *Id.* at 7.
 12. JOHN ICELAND, DANIEL H. WEINBERG & ERIKA STEINMETZ, U.S. CENSUS BUREAU, *RACIAL AND ETHNIC RESIDENTIAL SEGREGATION IN THE UNITED STATES: 1980–2000* tbl. 1 (2002). This index

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Scores above .60 are widely viewed as reflecting high levels of segregation. But in the large metropolitan areas where the black population is most concentrated, segregation levels persist at high levels reaching at or near .80 in New York, Chicago, Detroit, Milwaukee, and many other urban communities. Lower levels exist primarily in western and southwestern communities with small black populations. For Hispanics and Asians, segregation levels are much lower, approximately .4 and .5, but they have remained at that level or actually increased slightly between 1980 and 2000.¹³

Costs of Uneven Development

These patterns of development have adverse consequences for metropolitan areas. For residents of low-income and minority communities, a range of opportunities, including access to financial services, is limited.

Perhaps the most immediate costs result from both a skills and spatial mismatch. Those most in need of jobs (low-income residents of central city neighborhoods) lack the skills for, and live the greatest distance from, the areas where job growth is most highly concentrated.¹⁴

Health care services are particularly unevenly distributed. For example, in the affluent and predominantly white northwest side of Washington, D.C., and the neighboring suburb of Bethesda, Maryland, there is one pediatrician for every 400 children compared to one for every 3700 in the District's predominantly poor and black southeast side.¹⁵ In the predominantly black and Latino South Central Los Angeles community there is one primary care physician for every 12,993 residents compared to one for every 214 in the nearby wealthy community of Bel Air.¹⁶

The quality of public schools varies dramatically in large part because funding is based primarily on local property taxes. For example, in the 2002–2003 school year the city of New York (where 72% of the school population was black or Hispanic and 83% of the students were eligible for free or subsidized lunches) per pupil expendi-

varies from 0 to 1, where a score of 0 would indicate that each neighborhood had the same racial composition of the metropolitan area as a whole and a score of 1 would represent total segregation meaning every neighborhood was either all African American or all white. *Id.* at 5. For a more complete discussion of the index of dissimilarity, see Jeffrey M. Timberlake & John Iceland, *Change in Racial and Ethnic Residential Inequality in American Cities, 1970–2000*, 6 CITY & COMMUNITY 335, 335–65 (2007).

13. ICELAND, WEINBERG & STEINMETZ, *supra* note 12, at tbls. 3 & 5; *see also* John E. Farley & Gregory D. Squires, *Fences and Neighbors: Segregation in 21st Century America*, 4 CONTEXTS 33, 34–35 (2005).
14. *See generally* WILLIAM J. WILSON, *THE BRIDGE OVER THE RACIAL DIVIDE: RISING INEQUALITY AND COALITION POLITICS* (1999); WILLIAM J. WILSON, *WHEN WORK DISAPPEARS: THE WORLD OF THE NEW URBAN POOR* (1996); John F. Kain, *Housing Segregation, Negro Employment, and Metropolitan Decentralization*, 82 Q.J. ECON. 175, 179–189 (1968); John F. Kain, *A Pioneer's Perspective on the Spatial Mismatch Literature*, 41 URBAN STUDIES 7 (2004).
15. PETER DREIER, JOHN MOLLENKOPF & TODD SWANSTROM, *PLACE MATTERS: METROPOLITICS FOR THE TWENTY-FIRST CENTURY 77–78* (2d ed., rev. 2004).
16. MICHAEL K. BROWN ET AL., *WHITEWASHING RACE: THE MYTH OF A COLOR-BLIND SOCIETY* 14 (2003).

tures were \$11,627 compared to \$22,311 in suburban Manhasset (where 9% of the school population was black or Hispanic and 5% qualified for subsidized meals). Similar disparities prevail in most major metropolitan areas.¹⁷

When tragedies occur, it is usually low-income and minority communities that are particularly hard hit. Hurricane Katrina is a case in point. Damaged areas in New Orleans from Katrina were 46% black and 21% poor compared to 26% and 15% in other neighborhoods.¹⁸ One year after the storm, 23% of blacks, compared to 13.3% of whites, reported losing a job since Katrina hit.¹⁹ This is consistent with the effects of previous so-called “natural disasters.”²⁰

But it is not just distressed households and poor neighborhoods that pay. Ghettos and barrios in the nation’s metropolitan areas undermine the political stability, social development, and economic growth of the entire region. Cities with large poor populations and high levels of concentrated poverty pay more for a range of public services (including education, police, health care, and fire protection), increasing taxes and reducing their ability to attract middle-class families along with the resources they bring. Metropolitan areas with particularly high levels of income inequality grow more slowly than those where income is distributed more equally.²¹ In turn, the competitiveness of the nation’s economy generally is undercut. Uneven development is costly to all parts of many metropolitan areas and to the U.S. overall in an increasingly global world.²²

Uneven Development and Financial Services

The restructuring of financial services both reflects and reinforces these patterns of inequality and uneven metropolitan development. A two-tiered system of financial services has emerged, one featuring conventional products distributed by banks and savings institutions primarily for middle- and upper-income, disproportionately white suburban markets, and the other featuring high-priced, often predatory products, offered by such “fringe bankers” as check-cashers, payday lenders, pawnshops,

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17. See JONATHAN KOZOL, *THE SHAME OF THE NATION: THE RESTORATION OF APARTHEID SCHOOLING IN AMERICA* 321–24 (2005).
 18. JOHN R. LOGAN, BROWN UNIV., *THE IMPACT OF KATRINA: RACE AND CLASS IN STORM-DAMAGED NEIGHBORHOODS* 7 (2006).
 19. LOUISIANA RECOVERY AUTH. SUPPORT FOUND., *SOUTH LOUISIANA RECOVERY SURVEY: CITIZEN AND CIVIC LEADER RESEARCH SUMMARY OF FINDINGS* 11 (2006).
 20. See Michael P. Powers, *A Matter of Choice: Historical Lessons for Disaster Recovery*, in *THERE IS NO SUCH THING AS A NATURAL DISASTER: RACE, CLASS, AND HURRICANE KATRINA* 13–14 (Chester Hartman & Gregory D. Squires eds., 2006).
 21. BRUCE KATZ, BROOKINGS INST., *CONCENTRATED POVERTY IN NEW ORLEANS AND OTHER AMERICAN CITIES* (2008); Bruce Katz, Vice President and Dir., Metro. Policy Program, Presentation to the Fed. Res. Bank of New York’s “Housing in the New Marketplace” Conf.: *The New Urban Demographics* (Mar. 20, 2003).
 22. See DREIER, MOLLENKOPF & SWANSTROM, *supra* note 15; Dean Baker & Heather Boushey, *Trends in the U.S. Economy: The Evolving Role of Minorities*, in *SEGREGATION: THE RISING COSTS FOR AMERICA* (James H. Carr & Nandinee K. Kutty eds., 2008).

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and others targeted at low-income and predominantly minority communities concentrated in central cities.²³

One of the most dramatic changes in financial services has been the expansion of mortgage products. Just one generation ago most borrowers applied for a conventional loan and were either approved or denied. In recent years there have been dozens, if not hundreds, of products available in the market place. With the advent of risk-based pricing, lenders can offer an array of products priced in most cases according to the risk borrowers pose. So in addition to what was formerly a conventional or traditional fixed-rate thirty-year loan, there are many options including interest only, payment optional, variable rate, and many other loan types.²⁴ These so-called “nontraditional” mortgages accounted for more than one-third of all mortgage loans during the first nine months of 2006, compared to 2% just six years earlier.²⁵ The financial and broader economic crises of recent months have translated into less access to credit for many borrowers. Clearly, the proliferation of these new loan products, at least through most of 2006, has been a major contributor to what has become global economic turmoil.

A consequence of these developments has been a significant increase in high-priced, subprime mortgage loans which enable many families with blemished credit records to obtain a loan and become a homeowner who, just a few years ago, would not have been able to do so. There is no official definition of subprime loans, but basically they are loans to borrowers with blemishes on their credit records who could not qualify for conventional loans. But they are higher priced loans—that is, they involve higher interest rates or fees—to compensate lenders for the higher risk involved.

Subprime lending expanded exponentially in recent years, increasing homeownership for many families. Between 1994 and 2005, the annual dollar volume of such loans grew from \$35 billion to more than \$600 billion. This represented an increase from 5% to 20% of home-loan originations.²⁶ Homeownership rates reached record levels in recent years, which many attributed to the availability of subprime loans. But the argument that subprime lending increased homeownership has been challenged by recent research documenting that most subprime loans are for refinancing rather than purchase, and the number of families losing their homes as a result of

23. See JOHN CASKEY, *FRINGE BANKING: CHECK-CASHING OUTLETS, PAWNSHOPS, AND THE POOR* (1994); *MERCHANTS OF MISERY: HOW CORPORATE AMERICA PROFITS FROM POVERTY* (Michael Hudson ed., 1996); HOWARD JACOB KARGER, *SHORTCHANGED: LIFE AND DEBT IN THE FRINGE ECONOMY* (2005); JOHN P. CASKEY, BROOKINGS INST., *BRINGING UNBANKED HOUSEHOLDS INTO THE BANKING SYSTEM* (2002), available at <http://www.brookings.edu/es/urban/capitalxchange/article10.htm>; David Leonhardt, *Two-Tiered Marketing: Companies Are Tailoring Their Products and Pitches to Two Different Americas*, *Bus. Wk.*, Mar. 17, 1997, at 82.

24. ALLEN J. FISHBEIN & PATRICK WOODALL, CONSUMER FED’N OF AM., *EXOTIC OR TOXIC? AN EXAMINATION OF THE NON-TRADITIONAL MORTGAGE MARKET FOR CONSUMERS AND LENDERS* (2006), available at <http://www.knowledgeplex.org/showdoc.html?id=379601>.

25. Kristin Downey, *Mortgage Trapped*, *WASH. POST*, Jan. 14, 2007, at F1.

26. Robert B. Avery, Kenneth P. Brevoort & Glenn B. Canner, *Higher-Priced Home Lending and the 2005 HMDA Data*, 2006 FED. RES. BULL. A123.

default and foreclosure on these loans, which are often predatory, far exceeds the number who became homeowners.²⁷

If legitimate subprime lending has increased in recent years, it is also the case that many borrowers who would qualify for conventional loans are steered to even higher cost and often predatory loans. While there is no official definition of a predatory loan, most observers recognize that loans with the following characteristics are likely to be problematic:

- interest rates and fees that far exceed the risk posed by the borrower;
- loans with low initial “teaser” rates that adjust rapidly upward within two or three years and quickly become unaffordable for borrowers;
- high pre-payment penalties which trap many borrowers in unaffordable loans;
- loans based on the value of the property with little regard for the borrower’s income and, therefore, ability to repay;
- loan flipping whereby a loan is frequently refinanced, generating fees for the lender but no financial benefit for the borrower;
- high balloon payments; and
- negative amortization whereby the loan balance increases as borrowers make payments that are sufficient to cover only a portion of the interest but none of the principal that is due.²⁸

As a result of the debate over predatory practices, lenders were required to publicly report pricing information on selected high-cost loans beginning with their 2004 Home Mortgage Disclosure Act (“HMDA”) reports.²⁹ The HMDA, enacted in 1975, requires most mortgage lenders to disclose the geographic location, income, race, and other information for all loan applicants as well as whether the application was approved or denied. When the Federal Reserve Board analyzed pricing data at the time subprime lending was at or near its peak, researchers found that in 2006, 53.7% of blacks, 46.6% of Hispanics, and 17.7% of whites received high-priced loans.³⁰ In minority areas, 46.6% obtained high-priced loans compared to 21.7% in white communities.³¹

The controversy in recent years has focused on the following questions: Has predatory lending increased? Is it targeted at low-income and minority groups? What, if anything, should be done in response? While there is no data specifically

27. See, e.g., ELLEN SCHLOEMER, WEI LI, KEITH ERNST & KATHLEEN KEEST, CTR. FOR RESPONSIBLE LENDING, *LOSING GROUND: FORECLOSURES IN THE SUBPRIME MARKET AND THEIR COST TO HOMEOWNERS* (2006).

28. Elizabeth Renuart, *Housing Policy Debate: Market Failures and Predatory Lending*, 15 HOUSING POL’Y DEBATE 467 (2004).

29. See Avery, Brevoort & Canner, *supra* note 26, at A124. These “selected high-cost loans” are loans where the annual percentage rate exceeded that for Treasury securities of comparable maturities by three percentage points for first lien loans and five percentage points for second lien loans. *Id.* at A126.

30. Robert B. Avery, Kenneth P. Brevoort & Glenn B. Canner, *The 2006 HMDA Data*, 93 FED. RES. BULL. A73, A95 (2007).

31. *Id.* at A101.

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on predatory loans, news reports, community advocacy, research, enforcement activity pertaining to the rise, and uneven distribution of subprime loans have all increased dramatically in recent years.³² Clearly not all subprime loans are predatory, but virtually all predatory loans are in the subprime market.

The costs of predatory lending are severe. Families can lose their home and their life savings that went into purchasing the home. Short of such a cataclysmic event, predatory lending still costs families a lot of money—according to one estimate \$9.1 billion each year.³³ And the costs are not restricted to unfortunate individual borrowers. Many spill over into the neighborhood and metropolitan area. Subprime lending is concentrated in communities with high unemployment rates and declining housing values, constituting both a cause and effect of those neighborhood characteristics.³⁴ Econometric research has found that the recent rise in subprime lending is associated with higher foreclosure rates which in turn lead to higher crime rates, reduced property values, and, consequently, lower tax revenues.³⁵ To illustrate, the 3,750 foreclosures that occurred in Chicago in 1997 and 1998 reduced property values in neighboring homes by over \$598 million, an average of \$159,000 per foreclosure.³⁶

The Federal Reserve reported that 2.11% of residential mortgage loans held by banks were delinquent at the end of 2006, the highest rate since 2002 and at least twice as high as just one year earlier. Accordingly, real estate foreclosure filings have also been high. In April 2007, real estate foreclosure filings were up 62% over the 1.26 million filings in 2006, with more than two million households projected to lose their homes before the current mortgage crisis is over.³⁷ Several small lenders have failed, and large investors are shying away from investments backed by subprime loans. The explosive subprime mortgage market turned many mortgage bankers and brokers into millionaires seemingly overnight. When the Dow lost

32. See *Preserving the American Dream: Predatory Lending Practices and Home Foreclosures: Hearing Before the S. Comm. on Banking, Housing, and Urban Affairs*, 110th Cong. (2007) (statement of Sen. Chris Dodd (D-Conn.), Chairman, S. Comm. on Banking, Housing, and Urban Affairs); Chester Hartman, *Predatoriness, and What We Can Do About It*, in *WHY THE POOR PAY MORE: HOW TO STOP PREDATORY LENDING* 203, 204 (Gregory D. Squires ed., 2004) (citing a recent General Accounting Office report); Kristopher M. Rengert, *Editor's Introduction: Market Failures and Predatory Lending*, 15 *HOUSING POLY DEBATE* 449 (2004).

33. WEI LI & KEITH S. ERNST, *CTR. FOR RESPONSIBLE LENDING, THE BEST VALUE IN THE SUBPRIME MARKET: STATE PREDATORY LENDING REFORMS* 2 (2006).

34. Anthony Pennington-Cross, *Subprime Lending in the Primary and Secondary Markets*, 13 *J. OF HOUSING RES.* 31 (2002).

35. See Dan Immergluck & Geoff Smith, *The External Costs of Foreclosure: The Impact of Single-Family Mortgage Foreclosures on Property Values*, 17 *HOUSING POLY DEBATE* 57 (2006); Dan Immergluck & Geoff Smith, *The Impact of Single-Family Mortgage Foreclosures on Neighborhood Crime*, 21 *HOUSING STUD.* 851 (2006); Dan Immergluck & Geoff Smith, *Measuring the Effect of Subprime Lending on Neighborhood Foreclosures: Evidence from Chicago*, 40 *URB. AFF. REV.* 362 (2005).

36. Immergluck & Smith, *supra* note 35, at 57.

37. Peter G. Miller, *2 Million Foreclosure Filings in 2007?*, REALTYTRAC, May 31, 2007, <http://www.realtytrac.com/contentmanagement>.

more than 400 points one day in March 2007, over 200 points a couple of weeks later in that month, another 1,000 points in early August and another 4,000 points in 2008, at least a portion of those losses were attributable to growing problems in the subprime mortgage industry. And future declines were predicted by many due to continuing problems in the mortgage market.³⁸ But even these macro-economic effects are harshest in depressed communities, particularly the Gulf Coast and industrial Midwest. Subprime foreclosure rates in the fourth quarter of 2006 ranged from less than 3% in Washington, D.C., Maryland, and Virginia, to over 7% in Mississippi and over 9% in Indiana, Michigan, and Ohio.³⁹

Borrowers and their communities are taking great risks and paying substantial costs from recent developments in the mortgage market. That is less true for the industry. Originators can charge higher interest rates and fees, thus building additional risk into their business plans. Today most loans are sold in the secondary market, then packaged as securities and sold to investors. Risks, consequently, are spread across several actors. Again, when priced appropriately, originators and investors have profited from the proliferation of mortgage loans as many households and their neighbors have suffered.⁴⁰ The question remains: what should be done about the emerging two-tiered financial services industry and uneven development generally?

Past, Present, and Future Policy

Uneven development of the nation's metropolitan areas and inequities in housing and housing finance markets reflect a range of public policies and private industry practices. Among the factors that have structured the nation's housing markets, particularly the racial and economic composition of neighborhoods, are the following:

- intimidation and violence by neighborhood "improvement" societies to maintain the "character" of communities;
- explicitly discriminatory policies that virtually excluded non-whites from FHA and other government insured loan programs from the 1930s into the 1960s and fueled suburban development at the expense of central cities;
- refusal of real estate and rental agents to provide similar levels of service to white and non-white clients including steering of clients to communities based on their race and that of the neighborhoods;

38. Vikas Bajaj, *Freddie Mac Tightens Standards*, N.Y. TIMES, Feb. 28, 2007, at C1; Vikas Bajaj & Mark Lander, *Mortgage Losses Echo in Europe and on Wall St.*, N.Y. TIMES, Aug. 10, 2007, at A1; Julie Creswell & Vikas Bajaj, *A Mortgage Crisis Begins to Spiral, and the Casualties Mount*, N.Y. TIMES, Mar. 5, 2007, at C1, C4.

39. David Cho & Nell Henderson, *Where the Wolf Comes Knocking; Areas Already in Economic Distress Feel Rise in Housing Foreclosures Most*, WASH. POST, Mar. 15, 2007, at D1.

40. *Subprime and Predatory Mortgage Lending: New Regulatory Guidance, Current Market Conditions and Effects on Regulated Financial Institutions: Hearing Before the Subcomm. on Financial Institutions and Consumer Credit of the H. Comm. on Financial Servs.*, 110th Cong. 4-7 (2007) (statement of Allen J. Fishbein, Director of Housing and Credit Policy, Consumer Federation of America).

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- redlining by financial institutions (including the refusal to provide financing for many years and predatory lending more recently);
- concentration of public housing complexes in inner city ghettos and barrios; and
- exclusionary zoning ordinances in most suburbs that limit or prohibit multi-family housing and other affordable housing units.⁴¹

Individuals and families do make choices, but in a context not of their own choosing. It is unlikely that any progress will be made in addressing the inequitable access to financial services or exploitative practices generally if the structural sources of inequality are not addressed. If public policies and private practices have shaped the uneven development of metropolitan areas, including uneven access to financial services, then alternative policies and practices can ameliorate those patterns.

Several politically feasible tools are available to respond to the overall surge in inequality. For example, the federal minimum wage should be indexed to take into consideration the cost of living so that the recent increase that was approved in May 2007 does not continue to lose buying power as it has since the moment it went into effect in July 2007.⁴² Living wage ordinances, which mandate even higher wages, generally \$8 to \$10 per hour, frequently with fringe benefits, have been enacted in more than 100 jurisdictions with these rules applying to government contractors and recipients of economic development subsidies.⁴³ More jurisdictions should follow this lead. The Earned Income Tax Credit could be expanded to lift more working families out of poverty.⁴⁴ Enacting the Employee Free Choice Act, which allows workers to form a union when more than 50% of workers sign a card indicating their desire to do so in lieu of secret elections, would strengthen the role of unions in the U.S. and their positive impact on wage inequality.⁴⁵ A more provocative proposal, the Income Equity Act, has been offered by former Minnesota Representative Martin Sabo and would deny corporations tax deductions on any executive compensation exceeding twenty-five times the pay of the firm's lowest paid workers.⁴⁶

41. See KENNETH T. JACKSON, *CRABGRASS FRONTIER: THE SUBURBANIZATION OF THE UNITED STATES* (1985); DOUGLAS S. MASSEY & NANCY A. DENTON, *AMERICAN APARTHEID: SEGREGATION AND THE MAKING OF THE UNDERCLASS* (1993); DAVID RUSK, *INSIDE GAME OUTSIDE GAME: WINNING STRATEGIES FOR SAVING URBAN AMERICA* (1999); *THE GEOGRAPHY OF OPPORTUNITY: RACE AND HOUSING CHOICE IN METROPOLITAN AMERICA* 8 (Xavier de Souza Briggs ed., 2005).

42. See generally John Atlas & Peter Dreier, *Waging Victory*, AM. PROSPECT, Nov. 10, 2006, http://www.prospect.org/cs/articles?article=waging_victory; Neal Peirce, *Congress' Minimum Wage Vote: Prelude to a Better Politics?*, STATELINE.ORG, Jan. 25, 2007, <http://www.stateline.org/live/details/story?contentID=174954>.

43. Peter Dreier, *Community Organizing for What? Progressive Politics and Movement Building in America*, in *TRANSFORMING THE CITY: COMMUNITY ORGANIZING AND THE CHALLENGE OF POLITICAL CHANGE* 237 (Marion Orr ed., 2007).

44. See LAWRENCE MISHEL, JARED BERNSTEIN & SYLVIA ALLEGRETTO, *THE STATE OF WORKING AMERICA*, 2004/2005 13 (2005).

45. See THOMAS KOCHAN & BETH SHULMAN, *ECON. POLICY INST., A NEW SOCIAL CONTRACT: RESTORING DIGNITY AND BALANCE TO THE ECONOMY* 14, 14-16 (2007).

46. Peirce, *supra* note 42.

Expansion of several housing and land use policies would also reduce inequality. Inclusionary zoning laws that require developers to set aside a specific share of housing units to meet affordable housing objectives have been implemented in dozens of cities.⁴⁷ Tax-based revenue sharing, whereby a portion of the increasing property tax revenues in prosperous neighborhoods is used to invest in housing and other community development initiatives in distressed areas, has been implemented in Minnesota.⁴⁸ Mobility programs have enabled thousands of families to leave ghettos and barrios for more prosperous outlying urban and suburban communities where they found safer neighborhoods, better schools, and better job prospects.⁴⁹

Policies directed specifically at financial service providers are also required. Electronic banking makes it more cost-effective for mainstream institutions to serve the unbanked and out-compete the fringe bankers. Carefully targeted financial incentives, including tax breaks or CRA credit (see below), would encourage more banks to do so.⁵⁰ Community development finance institutions, which received incentives to serve traditionally underserved markets, appear to be doing just that. Such initiatives should be expanded.⁵¹

While financial literacy programs for consumers are helpful,⁵² more aggressive efforts to redirect the activities of mainstream financial institutions are essential to complement the efforts of alternative services, along with newfound consumer education. The CRA, a federal ban on redlining that requires mortgage lenders to ascertain and be responsive to the credit needs of their entire service areas, including low- and moderate-income communities, should be strengthened to provide sanctions for those that engage in predatory practices and credit for those that pursue equitable lending in their communities. Lender CRA records are taken into consideration when they submit applications to their regulators to merge with or purchase another institution or make any significant change in their business operation. Evaluation of CRA performance and its impact on such applications should reflect efforts to provide fair, equitable credit and to combat predatory lending. Currently

47. RUSK, *supra* note 41 (arguing that state legislatures must set new “rules of the game” requiring housing policies to ensure that all new developments have their fair share of low- and moderate-income housing).

48. MYRON ORFIELD, *AMERICAN METROPOLITICS: THE NEW SUBURBAN REALITY* (2002).

49. JOHN GOERING & JUDITH D. FEINS, *CHOOSING A BETTER LIFE?: EVALUATING THE MOVING TO OPPORTUNITY SOCIAL EXPERIMENT* (2003); ALEXANDER POLIKOFF, *WAITING FOR GAUTREAUX: A STORY OF SEGREGATION, HOUSING, AND THE BLACK GHETTO* (2006); LEONARD S. RUBINOWITZ & JAMES E. ROSENBAUM, *CROSSING THE CLASS AND COLOR LINES: FROM PUBLIC HOUSING TO WHITE SUBURBIA* (2000).

50. See Michael S. Barr, *Banking the Poor*, 21 *YALE J. ON REG.* 121, 221–36 (2004).

51. See HOWARD KARGER, *SHORTCHANGES: LIFE AND DEBT IN THE FRINGE ECONOMY* (2005).

52. *Id.*; *Home Mortgage Data: Hearing Before the Subcomm. on Financial Institutions and Consumer Credit of the H. Comm. on Financial Services*, 109th Cong. (2006) (statement of Douglas Duncan, Senior Vice President, Research and Business Development and Chief Economist, Mortgage Bankers Association).

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the CRA applies only to federally-chartered depositories (e.g., banks and thrifts).⁵³ This statute should be expanded to cover credit unions, independent mortgage bankers, insurers, and other entities that now account for well over half of all mortgage loans. The Community Reinvestment Modernization Act of 2007, introduced by Eddie Bernice Johnson (D-Tex.) and Luis Gutierrrz (D-Ill.), would accomplish this objective. In addition, the Home Mortgage Disclosure Act, which facilitates enforcement of CRA, should be expanded to include pricing information on all loans.⁵⁴

A strong national anti-predatory lending law should also be enacted. Currently thirty-six states and Washington, D.C., along with seventeen other local jurisdictions have such laws, leaving most consumers in other states less protected.⁵⁵

No doubt, more aggressive enforcement of fair housing and fair lending laws would also increase fair access to credit and banking services generally.⁵⁶ More provocatively, federal subsidies for homeownership (e.g., income tax deductions for mortgage interest and property taxes paid) could be withheld in segregated communities until their racial composition more closely approximated the region of which they are a part, thus making the fact of segregation, rather than the presence of non-whites, the problem to be solved.⁵⁷

A more fundamental change would be to place a duty of suitability on lenders requiring them to recommend loan products that are most appropriate for borrowers given their financial situation (reducing the likelihood of default and foreclosure), similar to rules that currently apply to securities brokers and financial planners. This, in essence, would shift at least some of the burden from individual consumers to lenders themselves to assure compliance with fair lending and anti-predatory lending rules. Some states are already moving in this direction by prohibiting those loan products and services that do not provide a net tangible benefit to the borrowers.⁵⁸

53. See Richard Marsico, *The 2004–2005 Amendments to the Community Reinvestment Act Regulations: For Communities, One Step Forward and Three Steps Back*, 39 CLEARINGHOUSE REV. 534, 534–45 (2006).

54. See John Taylor & Josh Silver, *The Community Reinvestment Act at 30: Looking Back and Forward*, 53 N.Y.L. SCH. L. REV. 203 (2008). Rep. Johnson and Rep. Gutierrez plan to introduce the Community Reinvestment Act Modernization Act of 2009 in January 2009. “Dear Colleague” e-mail from Rep. Eddie Bernice Johnson to John Taylor, President and CEO of the National Community Reinvestment Coalition (Nov. 19, 2008) (on file with New York Law School Law Review).

55. *Subprime and Predatory Lending: New Regulatory Guidance, Current Market Conditions, and Effects on Regulated Financial Institutions: Hearing Before the Subcomm. on Financial Institutions and Consumer Credit of the H. Comm. on Financial Services*, 110th Cong. (2007) (statement of Steve Antonakes, Massachusetts Commissioner of Banks); see also MORTGAGE BANKERS ASSOC., SUITABILITY—DON’T TURN BACK THE CLOCK ON FAIR LENDING AND HOMEOWNERSHIP GAINS 11 (2007).

56. See generally STEPHEN ROSS & JOHN YINGER, *THE COLOR OF CREDIT: MORTGAGE DISCRIMINATION, RESEARCH METHODOLOGY, AND FAIR-LENDING ENFORCEMENT* 15–95 (2002).

57. See JAMES W. LOEWEN, *SUNDOWN TOWNS: A HIDDEN DIMENSION OF AMERICAN RACISM* 442–46 (2006).

58. See Steve Covington, *Predatory Lending’s New Frontier*, MORTGAGE BANKING, Sept. 2005, <http://www.mbaa.org/files/Conferences/2006/Non-Prime/PredatoryLendingsNewFrontier.pdf>; see also Kathleen

In recent years several community groups and national membership organizations and networks have effectively challenged and changed the behavior of the financial services industry. Groups like the Association of Community Organizations for Reform Now (“ACORN”), the National Community Reinvestment Coalition (“NCRC”), the National Training and Information Center (“NTIC”), the National Fair Housing Alliance (“NFHA”), and others have secured access to financial services for markets that have long been underserved or exploited by the industry.⁵⁹ For example, ACORN estimated that between 1995 and 2004 it generated more than \$6 billion for low-income communities through its CRA organizing efforts and another \$6 billion from its anti-predatory lending campaigns.⁶⁰ Adding its work to create living wage ordinances, develop affordable housing, and reform various public services, ACORN pegs its return to low-income communities at more than \$15 billion.⁶¹ Using leverage provided by the federal Community Reinvestment Act, the NCRC estimates that more than \$4.7 trillion in new loans have been secured for low-income and minority markets since the statute was enacted in 1977 largely in response to community organizing efforts.⁶² Under authority provided by the FHA, the NFHA estimated that non-profit advocacy groups generated \$225 million for plaintiffs since 1990.

But future advances will likely require even stronger coalitions. There are a number of logical partners that come to mind, some of whom are already working with these community organizations. Organized labor, church groups, members of the local media, some elected officials (e.g., mayors whose cities are losing tax revenues from predatory lending), foundations, and many others have begun to collaborate in effective efforts to extend recent successes in democratizing access to financial services.⁶³

In what may be a sign of things to come, in January 2008, the city of Baltimore sued Wells Fargo Bank for targeting minority neighborhoods for predatory loans, thus constituting the first lawsuit filed by a municipality seeking to recover the costs associated with the resulting high foreclosure rates caused by such racially discriminatory lending practices (e.g., lost tax revenues, added fire and police costs, court

Engel & Patricia A. McCoy, *A Tale of Three Markets: The Law and Economics of Predatory Lending*, 80 TEX. L. REV. 1255, 1281–84 (2002); Patricia A. McCoy, *A Behavioral Analysis of Predatory Lending*, 38 AKRON L. REV. 725, 725–39 (2005).

59. ORGANIZING ACCESS TO CAPITAL: ADVOCACY AND THE DEMOCRATIZATION OF FINANCIAL INSTITUTIONS (Gregory D. Squires ed., 2002).

60. LISA RANGHELLI, ACORN, THE MONETARY IMPACT OF ACORN CAMPAIGNS: A TEN-YEAR RETROSPECTIVE, 1995–2004 12 (2006), available at http://www.acorn.org/fileadmin/Reports/ACORN_Wins_Report.pdf.

61. *Id.* at 2.

62. See FED. RES. BANK OF CLEVELAND, 30TH ANNIVERSARY OF THE COMMUNITY REINVESTMENT ACT 5 (2007), available at http://www.clevelandfed.org/Our_Region/Community_Development.

63. See Peter Dreier, *The Future of Community Reinvestment: Challenges and Opportunities in a Changing Environment*, 69 J. AM. PLANNING ASS'N 341, 342 (2003).

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administrative costs, social programs to maintain healthy neighborhoods, etc.).⁶⁴ Cleveland followed by suing twenty-one financial institutions for flooding the local housing market with subprime loans to people who could never repay, leading to a foreclosure crisis costing the city millions of dollars to maintain boarded-up homes and respond to increases in arson and other violent crimes. Whereas Baltimore is suing loan originators, Cleveland is suing financial institutions involved in mortgage-related investment activity.⁶⁵

The financial crises that many families (poor, working-class, and even middle-income) face are inextricably linked to broader forces of uneven development. The public policies and private practices that have generated these outcomes are no secret. Neither are at least some of the remedies.

64. See Complaint, Mayor and City Council of Baltimore v. Wells Fargo Bank, N.A., No. LO8CV 062 (4th Cir. Jan. 8, 2008).

65. Christopher Maag, *Cleveland Sues 21 Lenders over the Subprime Mortgages*, N.Y. TIMES, Jan. 12, 2008, at A9.