NATIONAL COMMUNITY REINVESTMENT COALITION NCRC

TESTIMONY

Testimony of

Josh Silver
Vice President of Research and Policy

On behalf of the
National Community Reinvestment Coalition

On the topic of
"Potential Modifications to Regulation C, Which Implements the Home Mortgage Disclosure Act"

Submitted to the
Federal Reserve Board of Governors
Washington, DC

Friday, September 24, 2010

National Community Reinvestment Coalition

727 15th Street, NW
Suite 900
Washington, D.C. 20005
Voice: 202.628.8866
Fax: 202.628.9800

NATIONAL COMMUNITY REINVESTMENT COALITION NCRC

The National Community Reinvestment Coalition (NCRC) appreciates that the Federal Reserve Board is conducting hearings and holding a public comment period on possible revisions to Regulation C that implements the Home Mortgage Disclosure Act (HMDA) data. The Board's 2002 revision to include price information for high cost loans and other data enhancements has increased transparency in the mortgage market. This has ensured a greater level of accountability for overall lending performance, and has enabled stakeholders to identify disparities in access to affordably-priced loans.

NCRC urges the Federal Reserve Board to make further enhancements to HMDA data. NCRC is an association of more than 600 community-based organizations that promotes access to basic banking services, including credit and savings, to create and sustain affordable housing, job development, and vibrant communities for America's working families. As an association of community-based organizations, NCRC and our member organizations use HMDA data regularly to assess whether institutions are meeting communities' credit needs consistent with safe and sound lending practices.

By increasing the public accountability of lending institutions, HMDA has made the lending marketplace more efficient and equitable. Further enhancements to HMDA data, however, are needed to enable HMDA to fully meet its statutory objectives of assessing whether financial institutions are meeting community needs and identifying possible discriminatory lending patterns. This week's release of the 2009 HMDA data indicates that significant racial disparities in denial rates and access to conventional loans remain that must be further investigated with enhanced HMDA data. In addition, improving HMDA pricing information is needed because, as acknowledged by this week's Federal Reserve Bulletin article, the imprecision of the pricing data impedes ongoing investigations of disparities in access to affordable loans.

Attached to this testimony is NCRC's recent report, *Foreclosure in the Nation's Capital*, which revealed the concentration of foreclosures and high-cost lending experienced by minorities in Washington DC, even after controlling for critical underwriting criteria and neighborhood characteristics.[1] This study, which combined HMDA data with a proprietary database, provides a glimpse at how much more effective HMDA data could be at identifying the possibility of potential discrimination and the extent to which credit needs are satisfied if it is enhanced in a significant manner.

We have identified the following improvements to HMDA that are critical:

[1] See http://www.ncrc.org/images/stories/pdf/research/ncrc_foreclosure_paper_final.pdf.

NATIONAL COMMUNITY REINVESTMENT COALITION NCRC

Necessary Improvements to HMDA Data

Additional information about loan terms and conditions

Information on points and fees, coupled with price information for all loans can help determine whether borrowers are receiving fairly-priced loans or loans that have exorbitant fees/and or annual percentage rates.[2] Price information for all loans is imperative for the purpose of identifying possible discrimination. As recent Department of Justice settlements suggest, price discrimination is often in the range of 50 to 70 basis points, meaning that such discrimination may occur entirely within the realm of prime lending. Currently, the publicly available data which only reveals prices for high-cost loans cannot be used to determine price discrimination in prime lending, which will be the predominant form of lending for the foreseeable future.[3] Moreover, as this week's Federal Reserve Bulletin article on the 2009 HMDA release suggests, the definition of a high-cost loan will likely remain uncertain. This means that price information for all loans is critical since the general public and researchers will be more able to discern significant price disparities by demographic category of borrower for a wider sample of loans than the currently narrow range of "high-cost" loans.

Reporting loan terms, such as the presence of prepayment penalties and whether the loan is fixed or adjustable rate, is also necessary to assess which borrower groups receive a disproportionate amount of onerous loans. The extent of income documentation (full or partial) would provide insight into whether the extent of income documentation correlates with default rates and which institutions are following responsible practices regarding documenting borrower income.

The loan channel (broker, correspondent, or retail) sheds light on which institutions are most likely to offer responsible loans and which offer problematic loans. In addition, information on yield spread premiums (YSPs), other forms of originator compensation, and loan channel will enable the Federal Reserve to determine if lenders and brokers are complying with the new Federal Reserve rules that prohibit varying YSPs and compensation based on loan terms and conditions. If more information had been available on loan terms and conditions several years ago, stakeholders could have identified troubling trends earlier such as a dramatic rise in option adjustable rate lending, and could have taken steps to curb this lending earlier before it contributed to the current crisis.

---

[2] Points and fees should be total points and fees payable at origination and required to be reported to the borrower by RESPA and TILA.

[3] See United States of America complaint against First United Security Bank, filed September 30, 2009. The price discrimination involved interest rate differences of 62 basis points between similarly situated African-American and white borrowers.

Information on critical underwriting factors

Additional information regarding underwriting criteria can help reveal if discrimination is occurring or if community needs are being met responsibly. Loan-to-value ratios (LTVs), debt-to-income ratios (DTIs), credit scores, and property values are variables that researchers need to account for when determining whether racial disparities in pricing or access are likely to be the result of discrimination.[4] In addition, more refined assessments of whether lenders are meeting community needs are possible if the data shows whether loan-to-value and debt-to-income ratios are reasonable and will contribute to sustainable loans or are too high and are therefore likely to result in unsustainable debt levels.

In its merger approvals, the Federal Reserve Board states that HMDA data is insufficient by itself to demonstrate if lending institutions engage in discriminatory practices. A typical discussion of HMDA data in Federal Reserve merger approval orders is:

> Although the HMDA data might reflect certain disparities in the rates of loan applications, originations, and denials among members of different racial or ethnic groups in certain local areas, they provide an insufficient basis by themselves on which to conclude whether or not the bank has excluded or imposed higher costs on any group on a prohibited basis. The Board recognizes that HMDA data alone, even with the recent addition of pricing information, provide only limited information about the covered loans. HMDA data, therefore, have limitations that make them an inadequate basis, absent other information, for concluding that an institution has engaged in illegal lending discrimination.

In order to realize the purpose of HMDA in identifying the likelihood of discrimination, the Federal Reserve Board and the Bureau of Consumer Financial Protection must considerably increase information on borrower characteristics and loan terms and conditions.

Testifying at the Federal Reserve hearing in San Francisco, David Moskowitz of Wells Fargo indicates that it is necessary to add "several established risk factors such as credit score, debt-to-income ratio, and loan-to-value ratio," to the HMDA data in order to enhance public understanding of lending decisions. NCRC agrees and also adds that this information is necessary for enforcement activities.

Even if after enhancements to the data, the data still cannot conclusively identify discrimination, enhanced HMDA data will nevertheless reveal much more clearly those institutions that treat similarly situated borrowers differently and offer them varying terms and conditions. For example, if the enhanced data has elements such as credit scores, LTVs, DTIs, and more pricing information, then the data will be much more effective in determining if a bank is treating similarly situated borrowers differently. Even if the data does not prove discrimination, it can identify if one of the banks involved

[4] Reporting both LTVs and Combined Loan to Value ratios would be desirable. To report CLTVs, HMDA data would have to link first and second liens in cases when a borrower received both first and second liens.

in a merger application is an outlier in terms of different treatment of similarly situated borrowers. The regulatory agencies will then be justified in denying the merger application or issuing a conditional approval requiring specific improvements in fair lending performance. Enhanced HMDA data would also improve fair lending reviews on CRA exams and could lead to either lower ratings and/or mandated improvements in CRA and fair lending performance when warranted. With HMDA data in its current form, the Federal Reserve Board has not come close to realizing the potential of HMDA data in achieving its purpose of identifying and eradicating discriminatory practices.

Loan performance data linked to HMDA data:

Loan performance is an important indication of whether lending institutions are meeting community needs. After a loan is delinquent, the publicly available data should indicate whether the institution modified the loan and if so, the extent of the modification (for example, how much was the principal loan amount reduced). The Dodd-Frank financial regulatory reform bill includes both loan performance and modification data, but it does not include data for modifications outside of the HAMP program. All types of modifications should be reported. Data on loan performance and modifications are important for CRA exams. If a bank, for example, is an outlier in terms of very high default rates and does not attempt to modify a significant number of loans, it should receive a low or failing rating on a CRA exam because it is not meeting credit needs in a safe and sound manner.

HMDA data is missing certain loan types

Some loan types have had an inconsistent track record in helping to meet credit needs in a responsible manner. For example, home equity lending is currently an optional reporting item for HMDA. Since unscrupulous home equity lending was one form of problematic lending that exacerbated the current foreclosure crisis, reporting home equity lending in HMDA data should be mandatory. Likewise, reverse mortgage lending has been frequently used in an irresponsible fashion, and mandatory reporting in HMDA data would help to identify and curb such abuses. In addition, NCRC agrees with the California Reinvestment Coalition that the multifamily data in HMDA could be significantly improved in order to reveal if lending institutions are meeting credit needs for rental housing. In particular, the multifamily lending data lacks information regarding whether the loan was for a purchase of a multifamily property, a refinance of an existing multifamily loan, or for improving the multifamily property.

Demographic Information Needs to be Improved

NCRC appreciates that the Dodd-Frank bill will require HMDA data to include the age of the borrower. This information will enable stakeholders to more precisely measure disparities in lending related to the age of the borrower. During the peak of subprime lending, stakeholders were concerned about a disproportionate amount of high-cost lending being targeted towards senior citizens. Yet, the best proxy that could be used with HMDA data was examining levels of lending by age of residents in census tracts. NCRC found that neighborhoods with high percentages of elderly residents had high levels of subprime loans, even after controlling for housing stock characteristics and borrower creditworthiness.[5] However, more precise measurements are needed, making the addition of age in HMDA data an important data element.

Along the same lines, NCRC supports the request from our member organization, the California Reinvestment Coalition, to add distinct categories of Asians in HMDA data. It is very likely that the borrowing experiences of more recent immigrants such as the Hmong are quite different than Asians like the Chinese or Japanese that have been in this country for generations. The current HMDA data, however, cannot capture these differences. In addition, the experiences of English speakers compared to speakers of another language are most likely to be quite different. HMDA data should have a data field indicating if English is the primary language of the loan applicant.

Loopholes and gaps in HMDA data collection need to be addressed

The reporting of parent institutions is currently not mandatory in HMDA data. This information is critical for the public to know whether an institution as a whole or whether its affiliates are engaged in responsible or reckless lending. Currently, a researcher or community group has to use bulky PDF files from the website of the Federal Financial Institutions Examination Council to identify which affiliates and subsidiaries are owned by a particular holding company. The website, moreover, is not completely reliable and contains these records for only the two most recent years. It is almost as if this system is designed to obscure or at least make quite difficult figuring out who owns which institutions. We urge the Board to fix this needless difficulty by including in the HMDA data fields identifying if the particular lender is owned by a parent institution and the name of the parent institution.

In addition, HMDA data for rural areas and smaller metropolitan areas is incomplete since only depository institutions that report CRA small business or farm loan data are required to report HMDA data in rural counties and for geographical areas beyond their branch network. This gap should be closed by requiring any HMDA reporter to report all loans they issue in all geographical areas. Finally, any institution that goes under in a given year should be required to report any HMDA data for that year. Recently, some failures of large subprime lenders resulted in a significant amount of missing HMDA data because they were not required to report data in their last year of operation.

HMDA's coverage of lending institutions should be increased in order to provide a complete picture of the number of lending institutions serving communities and their varying abilities to meet credit needs. The purpose of the statute in assessing if credit needs are met can be best realized if HMDA data covers the great majority of lending institutions. If a significant amount of institutions with a sizable number of loans are not HMDA reporters, stakeholders and researchers will not be able to determine the extent to which the lending industry is serving various borrowers and communities. In addition,

---

[5] NCRC Broken Credit System report, available from NCRC upon request.

any possible discriminatory practices of the omitted lenders cannot be detected, thwarting one of the essential purposes of HMDA.

NCRC reinforces our point about more complete coverage of lending institutions by quoting from the testimony of William A. Loving, Jr. President and CEO of Pendleton Community Bank at the Federal Reserve hearing in Atlanta this July.

> Obtaining HMDA data from only a subset of mortgage lenders that provide mortgage services to a specific segment of the market does not give regulators an accurate picture of mortgage lending patterns. I believe that the only way to determine an accurate portrayal of the mortgage practices in a particular area or market is to require HMDA reporting of mortgage brokers, non-lender loan purchasers and originators that meet the threshold criteria. Not only does this provide a consistent overview of the mortgage market, but ensures that discriminatory lending patterns are uncovered from any mortgage source.

The Federal Reserve's regulations for non-depository institutions have confusing rules regarding HMDA reporting requirements. The current regulation refers at different points to assets, percent of loans, and number of loans for determining if non-depository institutions are HMDA reporters. The rule should be simplified to establish a reporting requirement if a non-depository institution makes 50 or more HMDA reportable loans. Fifty loans is generally an acceptable threshold for making statistically significant observations regarding whether a lender is engaged in possible discriminatory activity.

The HMDA reporting threshold should be the same for depository institutions as for non-depository institutions. Fifty loans is a reasonable threshold for all institutions. While the threshold rules for depository institutions are asset-based and established by statute, the Federal Reserve Board can recommend that Congress change these reporting rules.

Public Access to HMDA Data

Increasing public access to user-friendly data enhances economic democracy and the ability of the public to hold lenders accountable for serving credit needs in a responsible fashion. If the data remains primarily the plaything of academics, its usefulness in bolstering access to credit is curtailed. On the other hand, if several community groups and other members of the public can tabulate some basic and important information with the data and use the data in meetings and discussion with lending institutions, the data is more effective in motivating lenders to increase responsible lending to underserved communities.

The data that is publicly available from the website of the Federal Financial Institutions Examination Council must be more user-friendly. The data should be available in excel tables in addition to the PDF tables. Excel tables would increase the ability of community groups to use and analyze the data. The Federal Reserve Board should consider adding a feature to the website that would allow users to query the database. For example, the website could allow the general public to calculate the percent and number of prime and high-cost home purchase loans made to various borrower groups by a particular lender in a particular census tract or in a county. While the Federal Reserve would be hesitant to compete against private vendors that provide these types of services, some basic queries would be very useful.

The Federal Reserve Board should also prohibit lending institutions from providing the data in formats that are not usable to community groups and members of the general public. NCRC and our member institutions have received HMDA data in PDF format, making it impossible to use, particularly for large lenders that issue thousands of loans. The Dodd-Frank Act requires lending institutions to submit the data in a format prescribed by the Bureau of Consumer Financial Protection. The Federal Reserve Board must immediately adopt this provision and decree that lenders submit data to the public in excel or other reasonable formats requested by members of the public. Moreover, financial institutions should not be allowed to charge fees to nonprofit organizations or individual citizens.

The Federal Reserve Board must also improve the timeliness of releasing the data. Before the introduction of pricing data, HMDA was released in August of each year. Now, it seems as though the data is being released later and later towards the end of September. Since the pricing data is no longer new, the release of HMDA should be closer to end of August. Moreover, the Federal Reserve should explore whether it is possible to release some data every quarter or once every six months. The lag in receiving the data means that the general public is receiving data that is almost two years old, making it difficult to determine if lenders are meeting needs as well now as they were several years ago. The time lag frustrates HMDA's statutory purpose of assessing if credit needs are being met.

Technical Issues

When considering HMDA enhancements, certain technical issues are complex but can be surmounted through thoughtful analysis. For example, various lenders use different credit scores which range from their own proprietary credit scores to FICO scores. Enhanced HMDA data could include one categorical data field that indicates if the credit score relied upon to evaluate the borrower's application was proprietary, FICO, or some other score. This field could also accommodate a category labeled "alternative credit scores" which are developed based on records of paying utility bills and rents. Then an additional data field would indicate the quintile of risk that the credit score assigned to the particular borrower. Since credit scores have different numerical ranges, the quintile of risk standardizes reporting to some extent. Moreover, a robust analysis using a variety of the HMDA data elements and comparing quintiles of risk assigned by the various credit score models in the HMDA data will provide insights into which models are accurately assigning borrowers to risk quintiles and which systems might be running afoul of fair lending laws in their assignment of borrowers to risk quintiles.

Another complex technical issue relates to the definition of income and debts when considering the collection of income and debt-to-income ratios in HMDA data. Lenders commonly use relied upon income which may differ from a borrower's income by excluding rental income or other sources of income. The Dodd-Frank Act may aid in the development of standardized income reporting; it requires lenders to use IRS W-2 forms, tax receipts and payroll receipts in determining a borrower's income. In addition, the definition of debt varies across the industry and for conventional and government-insured lending. The Federal Reserve could research the various definitions and attempt to develop a standard definition that reflects the common elements of the various definitions and that incorporates a comprehensive measure of debt.

While standardization of income, debt, and other data is desirable, the Federal Reserve should not base its decision on including a new data element on whether standardization is possible. For example, if it is not possible to completely standardize the definition of debt, the Federal Reserve should still collect debt-to-income ratios. It is unlikely that the definition of debt will be so completely different as to render the data difficult to compare across lenders. In addition, the data would still be valuable in identifying unsafe and unsound practices such as whether any particular lenders or group of lenders are making loans with unusually high debt-to-income ratios.

Parcel numbers and universal loan identification numbers required by the Dodd-Frank bill will be very helpful in linking the current HMDA data to loan performance and modification data required by the Dodd-Frank bill. It will also make it possible for HMDA to become a longitudinal database measuring loan performance over time. The originator identification required by Dodd-Frank will be quite helpful in adding loan channel information into the HMDA data.

Privacy Considerations

An argument made against enhanced HMDA data is that the improvements will increase the ability of unscrupulous companies or individuals to identify the actual borrower receiving the HMDA reportable loan. Unscrupulous lenders may then push-market high cost loans or other risky loans to vulnerable borrowers with low credit scores. These familiar arguments ring hollow. Currently, the financial industry has detailed data on consumers including their credit scores and loan history. Moreover, there are methods for enhancing the data that make it less likely for unscrupulous actors to use the data for malevolent purposes. For example, converting actual credit scores into quintiles of risk make it more difficult to identify a specific consumer. While NCRC urges loan level disclosure, another possibility is to disclose the most sensitive variables on a census tract basis, which also thwarts the unscrupulous actors.

Priorities for the Federal Reserve Board

Because the Dodd-Frank financial regulatory reform bill addresses some data issues, we recommend that the Federal Reserve Board prioritize data elements not required by the bill. For example, debt-to-income ratios and mandatory reporting of home equity and reverse mortgages are not required by the bill. In addition, non-HAMP modifications are not required to be reported under the bill. Nor does the bill address the current gaps in

HMDA data reporting such as the identity of the parent institution and incompleteness in rural areas. These items may therefore be towards the top of the Federal Reserve's list of enhancements. Yet, we also suggest that the Federal Reserve should not focus only on items excluded from Dodd-Frank. Loan-to-value ratios, pricing information for all loans including points and fees, credit scores, loan performance information, and other Dodd-Frank elements are also extremely important.

Conclusion

The Federal Reserve Board's consideration of HMDA data is vital. Enhancing HMDA data is needed so that HMDA can more fully realize the statutory goal of assessing if credit needs are met and if discrimination is present. NCRC urges the Federal Reserve Board to engage in a rulemaking to improve HMDA data, and in so doing, to improve the equity and efficiency of the marketplace.

Thank you for this opportunity to testify on this important matter.

NATIONAL COMMUNITY REINVESTMENT COALITION NCRC

Foreclosure in the Nation's Capital:

How Unfair and Reckless Lending Undermines Homeownership

NCRC DISPARITIES IN LENDING SERIES