<u>Record of Meeting</u>
Community Advisory Council and the Board of Governors
Friday, May 26, 2017

1. **Current Market Conditions:** *What is the Council's view of the current condition of, and the outlook for, loan markets and financial markets generally? Has the Council observed any notable developments since its last meeting for loans in such categories as (a) small business, (b) home mortgage, (c) multifamily and affordable housing, and (d) consumers? Do Council members see economic developments in their regions that may not be apparent from the reported data or that may be early indications of trends that may not yet have become apparent in aggregated data?*

Proposals from the New Administration Threaten Equitable Economic Growth: While capital markets have shown continuing signs of strength, recent budget proposals and executive actions by the new Administration, if enacted, would severely constrain capital flow into low- and moderate-income (LMI) communities. Proposed cuts to health care, food assistance, and significant cuts in taxes for the wealthy will exacerbate disparities in wages, borrowing, affordable housing finance, and employment across major demographic segments and regions. Moreover, a large portion of consumers of the future are going to be people of color. For example, 7 out of 10 new households over the next 10 years will be households of color. If we do not have the proper financial tools, resources, and support mechanisms for these communities, there is a risk to the vitality of these communities and a risk to the vitality of our national economy. Failing to address these disparities, particularly in segments that are driving the demographic growth in our nation, will likely result in national level economic consequences, including lagging economic productivity and reduced GDP.

Immigration Enforcement Having Adverse Economic Impacts: Radical changes in immigration policy and enforcement are adding to market uncertainty, reinforcing economic disparities for LMI immigrants and further degrading the capacity of our economy to harness the economic dynamism that immigrants have always brought to our country. There are clear signs of disruptions in industries that rely heavily on immigrant labor (e.g., agriculture and service industries such as restaurants, hospitality, and health care—among others) as well as among immigrant entrepreneurs. These impacts are likely to translate into dampening economic activity, as well as into higher consumer prices for products such as chicken, pork, and domestically produced vegetables. The most dramatic impacts, however, will be on those people least likely to be reflected in official economic data produced by the Bureau of Labor Statistics.

Aggregate Data Masks Geographic and Racial Disparities in the Economy: Despite signs of strength and growth in aggregated data, there is persistent and perhaps even worsening anger among Americans living in marginalized communities across rural, suburban, and urban regions about their economic position. In far too many areas of persistent poverty, jobs are still too scarce, the standard of living for many LMI workers remains precarious, and income inequality continues to rise. Various market forces continue to exacerbate poverty and wealth inequities across the country, and many regions still have fewer jobs than before the Great Recession. Reasons for this include barriers to markets, the limitations on credit reporting, interstate highways, lack of public transit, and lack of broadband and other infrastructure. For instance, the loss of coal jobs across central Appalachia has contributed to the comparative lack of employment opportunity. Additionally, population shifts toward cities reflect the fallout from many economies built largely on extractive industries and agriculture, and has created a widespread phenomenon of urban and suburban poverty that resembles concentrated rural poverty. This has expanded the number of regions of concentrated, racialized poverty in unprecedented ways across the United States. The trend is obscured by aggregate data that points to overall strength and economic growth.

Small Business Lending Still Struggling to Recover: Bank small business lending in amounts of $100,000 to $500,000—the amounts generally necessary to create jobs and grow small businesses and microbusinesses—has not recovered since the recession. Loans below $100,000 are originated and funded by alternative service providers, including fintech companies—some of which engage in predatory practices. Commercial banks are increasing the number of partnerships with fintech companies in order to make smaller Community Reinvestment Act (CRA)-eligible loans more cost-effective. With regard to fintech companies, the Office of the Comptroller of the Currency (OCC) and other regulators have responded with a set of proposed charter rules. The Council urges that borrower repayment capacity be made part of the OCC's supervisory requirements to address abuses (to date) and give small businesses the capital they need.

Small Business Lending in Minority Communities Faces Challenges; Can Benefit from Minority-Led Lending Institutions: Small business lending may have leveled off in many regions, and access to capital for small businesses continues to be a challenge for low-income, rural, and minority business owners.

There is increasing recognition that Community Development Financial Institutions (CDFIs), whose staff and leadership reflect the communities that they target, are particularly effective and important in delivering capital to minority and rural small business owners. Particular attention should be paid to organizations that show quality portfolio performance and demonstrate that 50 percent or more of their portfolio reflects a specific minority or rural community.

Large banks, like Chase and Wells Fargo, have established programs and funded activities that have targeted "CDFIs of Color." Chase's Pro Neighborhoods has created diverse collaborations that bring together disparate organizations to implement innovative programs that impact housing and small business opportunities in underserved communities. Wells Fargo has implemented the Diverse Community Capital Program, which seeks to invest $75 million into Latino and African American communities to leverage greater small business lending. Both programs seek to identify minority-serving CDFIs and community lenders to create greater capacity and borrower results.

Unfortunately, commercial banks continue to seek out larger, more-established business borrowers rather than the non-tech growth businesses more commonly owned by people of color and women. Small business loans represented approximately 40 percent of total bank loans in 1995, but had dropped to roughly 21 percent by 2016. Some banks have reduced or eliminated their volume of loans of less than $250,000—a serious concern given a Harvard study that showed 60 percent of small businesses seek loans of under $100,000 and more than 70 percent of small businesses seek loans of less than $250,000. Small Business Administration (SBA) loans to African American borrowers declined 47 percent between 2009 and 2013, even as overall SBA loan volume rose around 25 percent.

Data from California Reinvestment Coalition indicate that 90 percent of small business lending in California in recent years has been in the form of small business credit cards, and not loans. While banks still receive CRA credit for this type of lending, and it is useful to a degree, credit cards often have high fees and penalties for late or missed payments, including rate hikes, and cannot be used for payroll and other small business cash needs. This often leaves small businesses more vulnerable to predatory alternatives.

A recent report from the Economic Innovation Group (EIG), a research organization that has been tracking economic dynamism—the rate and scale of business growth and decline—in the United States, finds that an index of dynamism for the country continues to decline. Despite the overall decline, some states with growing metro areas benefit from vitality, or net new business formation. EIG researchers see a link between more vitality and larger numbers of foreign workers in a state, and note their belief that strong entrepreneurial activity among immigrants is a key ingredient in economic dynamism for states.

Challenges in Home Mortgage Finance: In 2016, levels of homeownership dropped to the lowest levels in 51 years at 63.4 percent, with much lower levels for black and Hispanic households. Many factors contribute to this trend, including high levels of student debt, barriers to the use of alternative credit data, down payment requirements and the continuation of high Federal Housing Administration (FHA) mortgage insurance premiums. The 25- to 34-year-old age cohort, which is the typical age group for first-time home purchases, is beginning to enter the home-buying market, but at later ages than earlier generations. The ability of households to buy their first home and achieve sustainable homeownership is highly dependent on addressing these factors and on the cost of housing in a given market. Although interest rates remain at historic lows, demand for mortgages by first-time homebuyers is highly dependent on the availability of for-sale homes that are affordable to first-time buyers.

New home mortgage applications and sales continue to rise.[1] An average loan size of $330,000 corresponds to average borrower income of $71,660. Existing sales are down, however, and the median existing-home price for all housing types in December rose to $232,200, up 4 percent, due to supply issues.[2] According to the National Association of Realtors (NAR), "Total housing inventory at the end of December dropped by 10.8 percent to 1.65 million existing homes available for sale, the lowest level since NAR began tracking the supply of all housing types in 1999." There continues to be a shortage of starter homes, particularly in high-cost markets along the coasts.[3] The opposite is true in the high-end home market. This reflects a need for new construction and construction loans at the trade-up and entry price points. The competition between for-profit investors for distressed housing as rentals appears to be increasing this mismatch.[4]

Furthermore, black homeownership is at historic lows, reflecting constraints on credit access, availability of starter homes, etc. Anecdotal evidence suggests that Latinos and immigrants—regardless of status—are not applying for credit due to new fears stemming from the Administration's policies on immigration. This is in addition to the rapid pace and high levels of gentrification that communities of color are facing in cities, leaving them priced out of their neighborhoods and losing social and cultural ties that can provide economic stability.

Contract-for-Deed Sales Seeing Resurgence: Media reports indicate resurgence in the practice of using contracts for deed as a financing mechanism. These contracts allow sellers (often investment firms that buy distressed property in bulk) to market to buyers who do not qualify for traditional mortgages, but with unfavorable terms. Contract buyers do not build home equity incrementally (as mortgagors do) or hold legal interest in the property until they have made all contractual payments. In the event of even one missed payment, foreclosure and eviction can take place within a very short period, and all prior payments and the property itself are forfeit. Contracts for deed are very hard to track and regulate, as unlike mortgages, states are not required to collect data on their use. Buyers must pay property taxes and often must effect costly repairs, but they have no legal ownership prior to fulfilling the final contract payment. The practice is most prevalent in communities still recovering from the housing crash, with over

[1] See www.mba.org/2017-press-releases/february/january-new-home-purchase-mortgage-applications-increased-92-percent-year-over-year.
[2] See www.mba.org/mba-newslinks/2017/january/mba-newslink-wednesday-1-25-17/residential/existing-home-sales-slide-to-finish-2016.
[3] See www.trulia.com/blog/trends/market-mismatch-q12017/.
[4] See www.stabilizationtrust.org/news/press-statement-fannie-mae-financing-blackstone-single-family-rental-acquisitions.

90 percent in non-white community census tracts in Chicago. Over 75 percent were in black communities in Chicago, according to Cook County, Illinois, records. This is happening in communities nationally.

PACE Loans Are Ripe for Abuse:[5] Property Assessed Clean Energy (PACE) loans allow for the financing of energy and other home or business upgrades to property. They are federally approved loans, administered through states, and enforced through counties. About $3.4 billion in PACE loans were made in 2016, from a nearly negligible number in 2012. Underwriting is linked to a property's equity and not the owner's credit score, creating potential hazard for borrowers. PACE loans range from $5,000 to $100,000, and are relatively low-interest loans. Borrowers with home equity who may not otherwise qualify for a loan are being put at particular risk of losing their homes if they miss a payment on the PACE loan, even if they are current on their first mortgage, which is subordinated once the PACE loan is in place. Failure to make a PACE payment can result in a lien being placed on the home, and later transferred to any future buyer. And as one article indicates, "payments on PACE loans are typically considered a [tax] assessment and added…to your property tax bill. That mechanism catches many homeowners by surprise."[6] PACE loans essentially turn contractors into loan brokers, with a vested interest in getting loans approved, but they are not trained or required to fully explain the terms and risks to consumers. The product is ripe for abuse and future problems for LMI communities and vulnerable borrowers, especially given the recent growth in popularity.

Incentives for Multifamily and Affordable Housing Are Being Undermined: The future looks challenging for the affordable housing development market. With the value of credits going down and interest rates going up, investors in Low-Income Housing Tax Credits (LIHTC)—the primary source of affordable-housing development financing—are less motivated to invest. Complicating access further is that some states' LIHTC scoring systems favor very large, new construction projects, resulting in a growing number of smaller, older rental buildings falling into serious neglect because owners do not have access to rehabilitation financing. This is particularly pervasive in rural communities.

Across the country, there are examples of banks pulling back on previous commitments to finance affordable housing due to the President's tax plan. LIHTC investors believe that tax reform, including the lowering of corporate tax rates, is likely to happen in the near term and have made major adjustments to tax credit pricing, averaging in the range of a 15- to 20-percent reduction. As a result, developers nationwide are reviewing development costs, negotiating with investors, and seeking assistance from state tax-credit-allocating agencies to determine if they can close the resulting financing gaps. Some projects that have received allocations of credits will not be able to move forward. Some allocating agencies have decided to delay 2017 allocations until more is known about tax reform. While some corporate investors are sidelined, at least some bank investors continue to have an appetite for lower-priced credits.

Banks should legitimately receive CRA consideration for investing in and lending to LIHTC housing projects. However, not all projects are the same and should not receive the same CRA weighting and recognition. A large 300-unit, new construction project for 60 percent of area median income (AMI) should not count the same for CRA purposes as one that is neighborhood-focused with set asides for special needs for 50 percent of AMI and below. Each state's scoring system needs to recognize this difference. Scoring needs to also take into account the project's impact on its neighborhood as well as the normal project-level factors.

[5] See https://moneytips.areavoices.com/2017/02/10/will-pace-loans-cause-the-next-housing-crisis/.
[6] Ibid.

A Mixed Story in Consumer Lending: Overall origination volumes were generally strong heading into the third quarter of 2016, with heightened competition for prime borrowers in many market niches. For riskier borrowers, however, a tightening that began in 2015 has continued.

Access to credit varies by state depending on policies related to loan amounts and rates. In California, for example, nonbank lenders are cited by California Reinvestment Coalition as pushing people to borrow loans larger than the $2,500 threshold to avoid the state's rate caps. In 2015, the California's Department of Business Oversight reported that over 290,000 loans between $2,500 to $4,999 and were made at over 100 percent APR.[7] Over 20 percent of all loans made between $5,000 and $9,999 (34,229 loans) were originated at over 100 percent APR. Recent payday lending rules instituted by the Consumer Financial Protection Bureau help address abuses, but they cannot impose a rate cap for these loans.

Innovations brought to market by fintech companies over the past several years have demonstrated the potential of marketplace lenders to expand access to credit, particularly for traditionally underserved consumers. However, the challenges for these companies in expanding across multiple states and their respective regulatory jurisdictions have hampered their ability to grow and offer greater access to uniform products nationally.

In an effort to establish a national regulatory framework to address this challenge and opportunity, the OCC announced in December 2016 its intent to establish a special purpose national bank charter for fintech companies, with an emphasis on supporting financial inclusion and ensuring that predatory actors do not enter the national banking system. In response to the announcement, the Conference of State Bank Supervisors (CSBS) voiced its strong opposition to this effort and sued to stop the OCC on the basis that it lacks the statutory authority to create a special purpose charter. At the same time, the CSBS acknowledges it has a role to play in "supporting innovation by minimizing friction in the state regulatory system" and has announced Vision 2020, a commitment that "state regulators will adopt an integrated, 50-state licensing and supervisory system, leveraging technology and smart regulatory policy to transform the interaction between industry, regulators and consumers."

2. **Impact of Underemployment on the Labor Market:** *Have the Council members observed a change in underemployment among the populations or communities they serve in recent years? If so, how has underemployment impacted these communities? What strategies have individuals taken to improve their employment outcomes?*

Realities of 21st Century Labor Market: While the top line unemployment rate has fallen to pre-recession levels, underemployment remains a fundamental challenge in the labor market. The meaning of full employment is clouded when large portions of the working-age population are underemployed. Consistent with unemployment patterns, underemployment is highest among populations that experience the greatest disparities in income, wealth creation, and economic mobility. Higher rates of underemployment today compared to pre-recession levels are due, in significant part, to employers restricting workers to fewer hours than they would prefer to work as well as the proliferation of "1099" or "gig-economy" jobs and automation.

The Council sees enormous challenges with underemployment in urban centers where individuals struggle with high cost of living and housing, and resort to working more than one job to make ends meet. Black and Latino workers are almost twice as likely as their white counterparts to be working part time when they would prefer full-time work. Minority women in particular are relatively more affected by the

[7] See www.dbo.ca.gov/Licensees/Finance_Lenders/pdf/2015_CFLL_Aggregated_Annual_Report_FINAL.pdf.

growth of involuntary part-time employment. In rural regions, a shift away from living wage, goods-producing jobs toward mixed-quality, service-providing jobs has had a large negative impact on the middle class and their families due to lower pay, fewer benefits, and less predictable schedules. Lower pay and less income squeezes household budgets—reducing individual and family well-being and hampering the local and national economy by depressing spending and overall economic demand.

Unpredictable schedules also have a negative impact on workers and their families. Being "on call" is disruptive to family life and can constitute a poverty trap, making it difficult to maintain good mental and physical health, obtain further education or a second job, and coordinate child care. Most employers of part-time workers typically want people to work upwards of 30 hours a week. Further, some employers only want workers for "prime hours," and others attempt to make it more difficult for the underemployed to have multiple jobs. Workers who are marginally attached to the labor force have also increased, with particularly negative consequences for black workers. Underemployed workers face an increased risk of depression, greater stress, and lower self-esteem and face additional obstacles to full-time employment.

Employers frequently reduce the number of full-time employees to avoid the cost of benefits and to lessen the impact of demand fluctuations. The practice spread to other sectors, including manufacturing, while unemployment was high during the recession. Conservative estimates place 20 percent of the United Auto Workers in the "second tier," in which workers are temporary, subject to call, and typically limited to 30 hours a week.

Over the last several years, there has been a steady increase in the number of taxpayers presenting at Volunteer Income Tax Assistance (VITA) sites with 1099 forms, documenting their non-employee compensation. Many of these taxpayers who participated in the gig economy in one form or another to supplement their income did so without a thorough understanding that the earnings from these endeavors represented taxable income, although no taxes were being withheld because they were viewed as contractors. The resulting tax implications can be a financially devastating tax bill for self-employment income.

The interaction between wages and public benefits for low-income people creates unproductive incentives to limit work hours in order to maintain eligibility for public benefits that produce a higher value for the household and greater stability than an increase in hours or hourly wage. There is a need for public policy to more fully recognize these dynamics and better enable workers to engage in full-time work without triggering financial penalties for the workers or their employer.

Among workers overqualified for their current jobs, the challenges for recent college graduates in obtaining jobs at their skill levels have been particularly acute. Black college graduates were particularly hard hit by the recession, with an underemployment rate reaching a high of 56 percent in 2013. Research on the long-term impacts of underemployment has found that the effects of being underemployed after graduating from college can last more than a decade.

Emerging Solutions to Workforce Challenges: All of these issues have significant implications for the Federal Reserve's mandate to pursue full employment. There have been long-term structural changes in U.S. labor markets, and innovations in science and technology have reshaped how we work. We have reacted to rising unemployment as a short-term emergency, but underemployment is the subsequent—and very real—growing crisis. We need data to pinpoint what the full costs of underemployment actually are in order to know what policies might be effective in helping those affected. Further, targeted fiscal policy is needed to address underemployment, including workforce investment and self-employment strategies, which are a common and important means to increase household income.

In response to the growth of involuntary part-time employment, advocates have sought to improve the quality of part-time work and connect underemployed workers with full-time jobs. For example, San Francisco passed the first municipal "fair scheduling" policy, requiring large retailers to provide advance notice of work schedules, compensate workers for schedule changes, and pay part- and full-time workers the same rates. San Jose voters approved the "Opportunity to Work Ordinance" in November 2016, requiring employers to offer extra hours to current part-time workers before hiring more part-time or temporary employees. And Washington, D.C., recently passed a policy that sets minimum basic hour standards (30 hours/week) for janitors in large commercial buildings. Workers in the gig economy are also organizing themselves to demand better pay and working conditions. After strong advocacy from the App-Based Drivers' Association, Seattle passed a law allowing drivers who work for app-based companies like Uber and Lyft to unionize, despite their status as independent contractors.

VITA sites and their volunteers are uniquely positioned to help taxpayers participating in the gig economy to understand their tax returns, and provide suggestions for how to prepare for the following tax year to minimize the financial impact. CFED's Taxpayer Opportunity Network (TON) is developing a training program for VITA volunteers to be rolled out later in 2017. This training program will provide additional guidance in preparing these types of returns as well as talking points to help taxpayers understand the tax implications of their supplemental income.

Finally, Council members continue to see challenges in hiring of individuals over the age of 50. Regardless of ethnicity, these individuals are finding it harder to get jobs even when they have obtained technical (or other skills) training. Businesses continue to seek younger workers to fill vacancies. AARP's BACK TO WORK 50+ connects struggling Americans 50+ with the information, support, training, and employer access they need to regain employment, advance in the workforce, and build financial capability and resiliency to prevent them from slipping into poverty later in life. BACK TO WORK 50+ is targeting 50+ job seekers at more than 20 sites across the country.

3. **Retirement Savings and Pensions in Communities:** *In the communities the Council serves, have changes in the economy impacted retirement savings and/or pensions in recent years? Is there a dichotomy between actual savings and perceived savings among individuals? What strategies, such as financial literacy education, have you found to be useful in closing these gaps?*

The Council Recognizes the Nation Is in a Retirement Crisis: The median retirement savings for all working age Americans, including those who do not own retirement accounts, is only $2,500. The low level of savings starts with the extent of household financial insecurity, as nearly 44 percent of all U.S. households and 61 percent of households of color are liquid-asset poor, meaning they have less than three months of savings to cover expenses if they lose their job or experience another major financial disruption. The numbers are even worse for retirement savings since the 2006 Pension Protection Act led to the rapid shift from defined benefit plans (pensions) to defined contribution plans (IRA/401k).[8] Since the Great Recession, the combined amount of savings in IRA's has increased, but this has not translated to increases in household retirement security.

According to the Employee Benefit Research Institute, only 66 percent of workers in medium and large businesses—and only 33 percent of workers in small businesses—even participate in employer-provided retirement plans. The Center for Retirement Research estimates that more than half of U.S. households and two-thirds of low-income households will not have enough income to maintain their pre-retirement

[8] See www.nirsonline.org/storage/nirs/documents/PPA2016/ppa%20issue%20brief%202016%20final.pdf.

standard of living. The National Institute on Retirement Security shows that 45 percent of working-age households (40 million households) do not own any retirement assets at all.

These numbers are even worse for households of color. Economic Policy Institute estimates show that in 2013, the median retirement savings for white households stood at $73,000, while African American and Latino households had a median retirement savings of $22,000.[9] And workers of color are less likely to work for an employer that offers a retirement benefit program.[10] Sixty-two percent of white workers have employers that offer some kind of retirement benefit plan, compared to 54 percent of black and Asian workers and only 38 percent of Latino workers.[11] People of color are less likely to own retirement savings accounts. Sixty-two percent of African Americans and 69 percent of Latinos do not have any assets in a retirement savings account. According to the Center for Global Policy Solutions, 74 percent of black Americans have less than $10,000 saved for retirement.

The disparity in both the prevalence and account balances across racial demographics underscores the ways in which our current retirement savings structure exacerbates the racial wealth gap and provides disproportionate benefits to higher-income families. This is the result of the structure of the tax code, which provides deep subsidies for retirement savings for higher-income Americans, who typically take advantage of itemized deductions, and little or no subsidy for lower-income Americans, who are disproportionately people of color.

One of the biggest barriers is lack of access to retirement plans—which has worsened over time and is especially a problem for low-income workers, employees at small businesses, and younger workers. In recent years, the federal government has taken steps to address these problems. The Obama Administration included an automatic IRA program and an expanded Saver's Credit proposal in its budget proposals, but Congress failed to act upon either. In his second term, President Obama directed the U.S. Department of the Treasury to introduce the myRA program, which created a safe, low-cost retirement vehicle for workers who lack access to a workplace-based retirement savings program. However, uptake for the program has been limited thus far.

There are some promising innovations in the marketplace with regard to low-fee investment services—many of which are driven by technology platforms. These innovations aim to make the market more efficient and ultimately increase retirement savings over time. More study is needed to determine the extent to which these innovations are closing the gap.

State-Based Retirement Programs—a Solution under Threat: A state-sponsored retirement plan with automatic enrollment in IRAs or other vehicles would improve the financial security of private-sector retirees in the future. Leveraging insights from behavioral economics, these programs use an opt-out model, which has been found to greatly increase participation rates. Workers would have the ability to opt-out of the program at any time and the default investment for these IRAs would be highly secure and safe. Currently, five states have passed legislation (California, Connecticut, Illinois, Maryland, and Oregon), with California's Secure Choice program the largest and most advanced. In California, nearly 7 million primarily LMI households would benefit from the program, the largest portion of which would be Latino households.

Transparency, simplicity, and financial education are key components of these programs. Many states are also exploring how to use these programs to improve the financial capability of workers. For example, Oregon has required its Treasury Department to study how financial literacy can be integrated into its

[9] Ibid, 10–12.
[10] Nari Rhee, *Race and Retirement Insecurity in the United States* (Washington, DC: National Institute on Retirement Security, 2013).
[11] Ibid, 3.

program. Such programs can also include an automatic escalation feature that increases the contribution amounts of employees over time to ensure that they are saving enough for retirement.

However, these programs are currently under threat by Congress. In late March and early May of this year, the Senate passed HJ Res. 67 and HJ Res. 66, resolutions that strike down important Department of Labor (DOL) regulations that made it easier for states and local governments to enact retirement programs for workers without employer-sponsored plans. The House of Representatives passed both resolutions earlier in the year, and the President is poised to sign them into law in the near future. The DOL rules were passed to provide clarity so that states and local governments could pursue these programs without fear of litigation or other reprisals.

In response to this congressional action, the states of California, Illinois, Oregon, and Vermont have affirmed that they are moving forward with their programs and have deployed the relevant services to assure legality of their actions. The Council supports expansion of the role of states in increasing retirement account access and savings.

Pension Programs at Risk: There are only seven cities or states nationwide with a fully funded pension. The private sector is also struggling, as a report points out that pensions of companies in the S&P 500 were over $375 billion underfunded at the end of 2015. The U.S. Treasury rejected a benefit-reduction plan proposed by the Teamsters Central States Pension Fund, which would have dramatically reduced benefits to retired members. The Treasury ruled that even those reductions would not save the plan, which is projected to be insolvent in 2025—the same year that the Pension Benefit Guaranty Corporation is expected to become insolvent.

In addition, Congress is having a heated debate over the Miners Protection Act, which would require payments for the pensions and health care of tens of thousands of coal miners. The United Mine Workers of America (UMWA) pension funds are the only ones that the federal government has committed to funding. There is now only a single active employee for every 13 retirees, and many mining companies have been granted relief from paying into the accounts under bankruptcy rules. The collapse of the UMWA pension fund on top of the sharp decline in the coal industry has created untenable inequities that will only be solved with long-term, patient investments in coal-producing regions.

Actual Savings vs. Perceived Savings among Individuals: Research from the Center for Retirement Security at Boston College shows that Americans' perceptions of their retirement preparedness are in line with what actual data projections show. However, roughly 19 percent of workers misperceive their retirement preparedness—meaning that they believe they will be more secure in retirement than they actually will be. There are several reasons that factor into why some are overconfident in their retirement preparedness; one reason is a "wealth illusion" that some may experience particularly as it relates to defined contribution plans. For example, some may see a 401(k) with a balance of $100,000 as ample without knowing that it translates to just $400 per month in retirement income.[12]

Strategies for Closing Gaps in Retirement Savings: The large gap in retirement savings is a structural problem driven primarily by stagnant real wages and the shift from defined benefits plans to defined contributions plans. The Council asserts that solutions to close these gaps must address these structural elements to be effective. We have also learned that standalone financial education does not actually lead to better financial security outcomes for low-income workers. In fact, a recent study documents that

[12] See http://crr.bc.edu/wp-content/uploads/2017/02/IB_17-4.pdf.

financial education is less effective for low-income workers.[13] However, we have increasing evidence that focusing on building financial capability, rather than "financial literacy" holds promise as a complement to structural interventions—as long as efforts to build financial capability are paired with actual financial behaviors, such as a worker starting to save retirement for the first time. Programs to encourage employers to integrate services and products to increase financial capability are succeeding in the workplace, especially with younger workers. And educational institutions are seeing success through age-appropriate financial programs and experiences.

There is also a pressing need to ensure the fiduciary responsibility of investment advisors and to scrutinize fee structures, particularly for management of retirement savings plans. The current review of the DOL Fiduciary Rule raises concerns about whether there are sufficient legal protections in place for the average person attempting to save for retirement. Due to the lack of knowledge about retirement savings, this rule is beneficial to savers.

4. **Community Development Activities:** *How have community development lending, investment, and services needs changed in recent years? Have banks increased or otherwise changed their level of community development activity based on these needs? What types of community development activities are hardest for banks to address?*

The New Administration's Approach to Domestic Economic Policy and the Federal Budget Is Producing Uncertainty in the Nation's Community Development Financial Systems: Under-resourced, LMI communities experience the twin challenges of constrained access to capital for community development purposes and limited capacity to deploy that capital to most effectively address community needs and opportunities. These challenges are amplified in rural and tribal communities. CDFIs and credit unions are critical pieces of our financial infrastructure along with Community Housing Development Organizations (CHDO). Community developers, whether for profit or nonprofit, are desperately needed in these communities.

Uncertainty as to the future of key elements of fiscal policy and tax policy that make up the fundamental basis for the community development finance system in the United States is significantly impacting access and pricing on a range of products that benefit LMI communities. For example, pricing on low-income housing tax credits has dropped noticeably since December 2016, creating financing gaps in many affordable housing deals. The rollback of an FHA mortgage-insurance rate cut in the first days of the new Administration has kept in place a cost-barrier for LMI borrowers for whom the private market is offering few or no other options than an FHA-backed loan. Further, the President's budget proposal includes the total elimination of funding for federal programs that form the bedrock of locally driven efforts to provide financial products and services that promote economic mobility, including the Department of Housing and Urban Development's Community Development Block Grant and HOME programs, the Treasury' CDFI Fund, and the Department of Agriculture's Rural Development programs. If these programs are reduced or eliminated, there is likely to be a cascade effect on CRA investment because many local CRA investment opportunities (affordable housing development and preservation, small business lending, consumer financial counseling, etc.) rely on these federal sources for their viability—and in many cases rely on the federal funding for a large portion of the equity in community development projects.

[13] See https://papers.ssrn.com/sol3/papers.cfm?abstract_id=2333898.

Rapid Changes in Labor Markets and Technology Require Adaptation in Community Development Activities: Many people have lost high-wage jobs and have had to move toward lower wages, temporary employment, and/or retraining. Predatory consumer financial schemes like payday lending, rent-to-own, and other high-risk lending are rampant. These market conditions, coupled with increased medical and student loan debt, mean that many homeowners and entrepreneurs are struggling to obtain credit for homes and businesses. Changes in labor market conditions also mean that short-term financial needs are increasingly crowding out longer-term asset building activities such as home buying and retirement savings. Community development practitioners and policymakers need to research and craft solutions to this liquidity crisis in order to stem wealth inequality.

There is currently a trend of consumers using technology to manage their financial lives. The Federal Deposit Insurance Corporation has published excellent reports on the demand for mobile banking technology and other innovative fintech tools that provide more user-friendly ways to manage matters of personal finance. However, the digital divide still persists in communities without access to broadband or other basic infrastructure, with low-income communities once again being left behind. Thus, a growing priority for the field must be to address this digital divide if we expect to increase financial inclusion meaningfully.

Consumer Financial Protections Are Threatened: There are active policy efforts to eliminate or degrade consumer financial protections and financial market oversight, including eliminating or weakening the authority of the Consumer Financial Protection Bureau, a review of the DOL Fiduciary Rule, and a variety of proposals to repeal portions of the Dodd-Frank Wall Street Reform and Consumer Protection Act. Loosening of consumer protections and reduction of financial market oversight were significant factors in the economic collapse that led to the Great Recession and will introduce greater risk into the market if this policy direction is pursued again. Regulators should be prepared to carefully scrutinize changing market behavior that follows moves to make consumer protections and financial market oversight more lax.

More Impactful Approaches to Meeting Community Credit Needs Are Emerging and Require Greater Recognition, Investment, and Regulatory Flexibility: Several approaches and initiatives are showing promise in improving credit availability and access in communities and would benefit from increased support.

- **Building financial capability.** The 2016 Update to the National Strategy for Financial Literacy, produced by the Financial Literacy and Education Commission (FLEC), recognizes that the provision of financial education alone is not sufficient to drive behavior change.[14] Instead, a broader view of financial capability that incorporates knowledge and skills development alongside access to products is necessary to have a greater impact on personal financial management and savings. Partnerships across a range of sectors—including workforce development programs for adults and youth, community health centers, employers and human resources professionals, retail companies, Head Start programs, and educational institutions—are needed to implement financial-capability products and services in support of these sectors' business goals or social missions. Furthermore, many banks are still focused on delivery of financial education in a more static, traditional way; while some banks offer a diverse range of high-quality, free financial education resources, there are few ways to directly link this education to account products that meet the needs of their communities.

[14] See www.treasury.gov/resource-center/financial-education/Documents/National Strategy for Financial Literacy 2016 Update.pdf.

- **Homebuyer education.** Traditional homeownership education courses, while an important part of the process, do not provide enough of the needed assistance for households to improve credit scores, repay debt, and determine whether homeownership is a feasible goal. One-on-one financial coaching focused on preparing for homeownership is a more in-depth approach that has proven to be impactful for aspiring first-time homeowners and potential buyers with credit challenges. And an approach that combines classwork and individualized coaching has shown the greatest success in helping the homebuyer.

- **Workforce development.** The Community Advisory Council has previously provided detailed recommendations regarding approaches to workforce development and the members continue to see a tremendous need for more effective workforce development in various communities. See past Council meeting records at www.federalreserve.gov/aboutthefed/cac.htm.

- **Alternative mortgage lending.** Regulatory requirements for mortgage lending that have come into place since the Great Recession have made it particularly difficult for community development organizations like Habitat for Humanity chapters to originate their alternative mortgage loans in a compliant manner. An exciting initiative being pursued by Twin Cities Habitat for Humanity addresses this issue while also expanding the number of households the chapter can serve in a given year. Habitat is partnering with a CDFI bank that will handle the actual mortgage originations and has also obtained a commitment from another community bank to purchase the mortgages on an ongoing basis for the next four years.

  Another example of alternative mortgage lending is the Nationwide Mortgage Collaborative (NMC), which is being developed by Springboard CDFI and is designed to significantly increase access to mortgage credit for LMI and other underserved market segments and communities across the nation. NMC will harness homebuyer activities of hundreds of local nonprofit housing providers across the nation by creating a sustainable and scalable mortgage solution that will rebuild the delivery system for underserved borrowers. Nonprofit mortgage lenders typically cannot generate a sufficient volume of mortgage originations to cover costs or to garner the attention of the traditional mortgage lending industry. By aggregating loan originations through the collaborative, NMC will be able to ensure consistency of loan quality, standardize loan processing and underwriting, and bundle loans for interested CRA lenders or for sale to the secondary market.

Positive Developments in Community Development Finance: There appears to be increasing utilization of 4 percent housing tax credits in many markets. This has been an underutilized financing tool, but is now producing thousands of affordable rental units. Also, as a source of new capital in support of community and economic development, outreach, and education should be provided to potential socially motivated investors to increase the amount of investment capital.

5. **Additional Matters***: Have any other matters affecting consumers and communities emerged from the work of the Council members that they want to present at this time?*

Several additional issues are important to LMI populations: health care, education, housing finance reform, data desegregation, and climate change. These areas have the potential to create greater inequality with long-term effects for our economy.

Health Care: Rising costs of health care and prescription drugs continue to be a burden for low-income families. Families with health care coverage still struggle with high medical costs, particularly prescription drugs. Many LMI families are increasingly anxious about the fate of their health care coverage under the Affordable Care Act, given the proposed plans for replacing it. Consistently, research has shown that LMI individuals and families spend proportionately more on health care expenses than higher-income households, which imposes additional burdens on their financial situation and puts them at risk of (1) sacrificing other basic needs; (2) reducing consumption of other goods and services; and (3) filing for bankruptcy.

Furthermore, unforeseen out-of-pocket health care expenses often drive families to file for bankruptcy, which impacts their credit and ability to borrow and build assets in the future. Proposed elimination of 180-days past due medical debt from credit scores will benefit LMI families that have struggled with unforeseen medical costs.

Additional concerns revolve around the loss of state Medicaid funds, and the potential for increased health care costs for those with preexisting conditions. The current health care insurance plan proposed by the House will adversely affect states' LMI populations, including the elderly. Regulatory and statutory changes are needed that allow Medicare and Medicaid to bid for the lowest drug price whether the purchases are from domestic or international providers.

Education: Educational success will help create a more productive economy while also expanding economic opportunity and mobility. Yet, the high cost of college makes many students—especially those from low-income families—feel like higher education is out of reach. Two particular aspects of education are highlighted below as other matters affecting many LMI communities: student debt and access to early childhood education.

- **Student debt.** Research shows that, in time, an investment in higher education eventually pays off. However, the payoff of investing in higher education varies greatly depending on whether one graduates with or without student debt. Student debt among low-income and minority students is high, especially when they enroll in small for-profit schools and end up with no degree or a degree that will not provide the earning power to service large amounts of debt required to finance their schooling. Some national accrediting agencies facilitate abuse of student borrowers by predatory, for-profit schools by allowing these schools/colleges to arguably defraud students, pushing them to borrow hundreds of millions of dollars from federal student loan programs that become revenue for for-profit schools. Additionally, a student who graduates with high debt levels may be forced to delay homeownership and may save less for retirement.

  Government guaranteed loan programs would benefit from implementing prudent lending guidelines to prevent over lending to prospective students. However, recent policy changes exacerbate these challenges. Presently, protections for people in default on their student loans have been revoked, potentially subjecting millions of borrowers to exorbitant fees. The Education Department has also proposed large cuts to subsidized loan and grant programs that have provided access to postsecondary education for low-income students.

  One potential solution discussed by the Council includes Children's Savings Accounts (CSAs). CSAs are a policy tool that may help level the playing field. CSAs restore equity in returns on investments in education, improve the life chances of disadvantaged students, and help combat wealth inequality by helping children and their families build college savings. To help accounts grow, and in addition to individual/family contributions, children receive incentives from third parties (e.g., government or nonprofits), such as initial deposits to open accounts and matches for deposits. CSAs are intended for purchasing an asset (e.g., postsecondary education); provide direct, monetary incentives (e.g., initial deposits, savings matches, benchmark incentives, prize-linked incentives, or refundable tax credits[15]); and restrict withdrawals from savings for non-asset purposes.

Research shows that children with college savings of as little as $1 to $499 (1) are three times more likely to attend college; (2) are four times more likely to graduate than those without any savings; and (3) have higher college expectations and see themselves as college-bound. Additionally, the Annie E. Casey Foundation estimates that children's accounts could reduce the racial wealth gap by 20 percent to 80 percent, depending on participation and investment.[16] Research has also demonstrated that parents will do for their children what they won't do for themselves, which means that CSA programs could also promote financial education for adults in a classic two-generation approach.

- **Early childhood education.** Access to high-quality, affordable early education programs has become an obstacle for LMI families to be able to secure full-time employment, particularly for female-headed households. Further, research shows that participation in early education programs increases a child's likelihood of graduating from high school, attaining a college degree, and being gainfully employed.[17] Thus, early education benefits children but is also a workforce and economic development issue. Early education subsidies are not keeping pace with the demand, and in many states, like Massachusetts, funding for subsidized slots and for universal pre-K are still lagging, leaving LMI families without sufficient resources to cover the rising costs of early education and depriving young children of a strong foundation for their future. New York City has proposed an expansion of universal Pre-K to include 3-year-olds. It will be important to closely follow the implementation of such proposals and their impact and benefits to all young children, including infants and toddlers.

Housing Finance Reform: The continuing availability of capital to support a stable and robust single-family mortgage market is critical to the success of households and communities. Nine years after the government-sponsored enterprises (GSEs) Fannie Mae and Freddie Mac entered conservatorship, Congress and the Administration have not yet addressed housing finance reform, and this leaves an immediate and urgent issue unaddressed.

The current agreement with the Treasury to continue the conservatorship requires the payment of earnings to the Treasury at a pace that will drain the GSEs of capital by early 2018. This will mean that if either of the GSEs posts accounting losses in any given quarter following the final payment to Treasury, the GSE will need to request funds from the Treasury. This would likely cause uncertainty and concern in investor markets and could threaten the stability of mortgage markets. If Congress is unable to agree on a path of financial services reform soon, it will be essential for the current agreement with Treasury to be renegotiated to ensure that capital is maintained at the GSEs to support potential losses.

Role of Federal Data Collection in Knowledge Creation: The value and impact of the data collection and analysis work of the Federal Reserve and other federal agencies cannot be overestimated in terms of its influence in informing best practices and policy across all aspects of our economy. Federal data undergirds the basic functions of government. At a foundational level, the Census Bureau's surveys, including the Survey of Income and Program Participation (SIPP) wealth study, are not only used to

[15] Does not include programs that offer tax deductions only, which may not be accessible for low-income families who do not have a tax liability.
[16] See www.aecf.org/m/resourcedoc/aecf-investingintomorrow-2016.pdf.
[17] See https://heckmanequation.org/resource/research-summary-lifecycle-benefits-influential-early-childhood-program/.

identify or diagnose inequality or poor economic outcomes, they also are used to allocate resources and design legislation. Unfortunately, the SIPP itself has been on the chopping block over funding twice: once in 2006 and again during 2013's government shutdown. Both times, major overhauls in the survey's processes and methodology were undertaken as a result of budget cuts, which have had an effect on the survey's timeliness and its ability to accurately reflect household outcomes and dynamics within/among states.

Among the Census Bureau's surveys, the SIPP is one of the more niche and expensive and, thus, less likely to be renewed if the bureau is forced to prioritize in the face of drastic budget cuts. Given the present uncertainty in the future of the bureau's leadership, and in the timely and efficient completion of the constitutionally mandated 2020 census itself, it is likely that future iterations of SIPP are in jeopardy. A few Census Bureau surveys—Business Dynamics Statistics, the SIPP, the Consumer Expenditures Survey, etc.—overlap with the priorities of the Federal Reserve, and could be incorporated into existing Federal Reserve surveys. The SIPP, in particular, is already a complement to the Federal Reserve's Survey of Consumer Finances (SCF), and expanding the SCF—such as to 20,000 to 30,000 households, which would provide a large enough base to do state-level analyses—would allow better identification of trends in wealth inequality across income, racial, and gender lines.

Climate Change: Climate changes such as sea level rise and industrial contamination have a nationwide impact. Sea level rise affects many coastal communities, including tribal and native lands, across the country. Streets near the coast and on barrier islands are flooding, especially at high tide. Contamination of the Biscayne aquifer in South Florida with salt water as a result of sea level rise is a serious possibility. Scientific analysis of this and other environmental issues is crucial. Low-income families and people of color are disproportionally affected. The impacts of income and wealth inequality, racial and ethnic discrimination, and climate change are overlapping. Many neighborhoods are negatively shaped by all three of these issues. More understanding of the data on these issues is needed that can then drive needed policy changes and action responses.