Record of Meeting

Community Advisory Council and the Board of Governors
Friday, November 3, 2017

1. **Mortgage Access and Finance Reform:** *How have changes in mortgage requirements, such as Qualified Mortgage/Qualified Residential Mortgage (QM/QRM) rules, impacted access to mortgage markets, particularly for low- to moderate-income (LMI) borrowers? How does the Council see potential government-sponsored enterprise (GSE) reform in the near future reshaping the mortgage markets?*

GSE Reform

The mortgage finance system in the United States does not provide fair access to large segments of our population. As described below, we can do better.

Ensuring Access to Affordable Housing and Mortgage Credit for LMI Populations

Even taking into account the sobering lessons learned from the recession, affordable homeownership remains the most important wealth-building opportunity for most LMI families.[1] A major long-term macroeconomic benefit will be achieved if our mortgage finance system effectively opens access to those populations that will make up the largest portion of the growth of the mortgage market in the coming decades.

The Council has previously placed significant emphasis on the need to disaggregate economic data in order to understand the glaring disparities that exist in wealth, wages, and economic well-being among racial, ethnic, and geographic segments of our population. The mortgage market requires similar analysis, particularly in light of the fact that growth in mortgage lending will derive largely from the ability of minority borrowers to access affordable and fair credit.

In a June 2016 article, the Center for Responsible Lending described the high stakes in GSE reform for access to mortgage credit for LMI households by demonstrating the dramatic differences in pricing for borrowers with different credit scores under different reform scenarios.[2] Further, Urban Institute research shows that mortgage credit remains very tight and disproportionately out of reach for minority borrowers.[3] Research produced by Fannie Mae identifies challenges for rural borrowers post-recession, and members of the Council identified the failure of our mortgage finance system to serve rural markets including Appalachia.[4]

Increasing access to affordable and sustainable homeownership for LMI borrowers can be best achieved with a combination of (1) buyer preparation through credit counseling and homebuyer counseling, (2) down-payment assistance to well-prepared LMI borrowers, and (3) more accurate assessment of risk through improved credit-scoring methodologies. There is ample evidence that demonstrates how quality counseling services for borrowers reduce the risk of delinquency.[5] But while there is significant capacity among mission-driven agencies to provide more high-quality buyer preparation, there is insufficient

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[1] See www.jchs.harvard.edu/sites/jchs.harvard.edu/files/hbtl-06.pdf.
[2] See www.responsiblelending.org/sites/default/files/nodes/files/research-publication/urbaninstitute_calhoun_wolff_jun2016.pdf.
[3] See www.urban.org/sites/default/files/publication/88826/quantifying_tightness_of_credit.pdf.
[4] See www.fanniemae.com/resources/file/research/datanotes/pdf/working-paper-102716.pdf.
[5] See www.freddiemac.com/news/blog/pdf/benefits_of_pre_purchase.pdf; www.neighborworks.org/Homes-Finances/Foreclosure/Foreclosure-Counseling/Congressional-Reports; and www.neighborworks.org/researchtracking.aspx?id=17892&nid=3c8914c5-fbdb-4e4e-b405-a9cfffc1d236.

investment in this important risk-mitigating service. A housing counseling program administered by the Minnesota Housing Finance Agency that provides culturally specific organizations with up to $2,000 per household for intensive credit and homebuyer counseling is an example of a program that has shown early promise in opening access to mortgage financing, particularly for households of color. Further, down-payment assistance can open access for an otherwise qualified borrower who, without help, would take far longer to achieve a first-time home purchase. We must recognize that the most widely used legacy credit-scoring systems, which are often the primary method used by financial institutions to measure the potential risk of extending credit to a borrower, do a poor job of differentiating risk profiles among many borrowers that are LMI, black, Hispanic, Asian, and/or are immigrants.

GSE reform must allow risk to be reasonably pooled in the secondary market and should limit the centrality of risk-based pricing in any approach to reform. Risk-pooling advances broader economic mobility by allowing lower-income borrowers to access the same rates as higher-income borrowers. We also need to examine the implications of risk-based pricing and the hyper-segmented treatment of risk in the mortgage market. The data used for estimating risk is not sufficiently free of bias to reliably support hyper-segmentation that results in higher costs for those that appear to be higher risk.

Broader Systemic Reform

The Council recognizes the critical need for a resolution to the conservatorship of Fannie Mae and Freddie Mac. The Council is also conscious that mortgage-backed securities are the largest asset class in the global financial market and that change to the GSE infrastructure in the United States carries significant risk.

Many proposals have called for Fannie Mae and Freddie Mac to be rechartered to entities that are operated and regulated in a manner akin to utilities. In such a system, the rechartered entities, as well as any new entrants to the market, would perform many of the functions performed by the GSEs today with stronger oversight. There are also proposals for recapitalization and reform that call for the Federal Housing Finance Agency (FHFA) to implement a capital-restoration plan.[6] Once the GSEs build sufficient capital, they could be released from the conservatorship and begin operating again as private entities, but would remain under the supervision of a strong regulator, the FHFA.

There is growing consensus around a number of key principles for GSE reform:

- strong, independent oversight
- a strong commitment to enforceable affordable housing goals and the Duty to Serve requirements in the GSE charters in order to produce affordable ownership and rental housing options in all geographies
- broad availability of the 30-year, fixed-rate, prepayable single-family mortgages
- scaled multifamily finance programs that provide liquidity for rental housing
- private capital as first loss ahead of any explicit government guarantee on mortgage-backed securities
- a primary mortgage market served by lenders of varying sizes and business models
- a competitive secondary mortgage market that is responsive to the needs of the primary market
- an orderly transition from the current system to the reformed system

[6] See www.housingwire.com/ext/resources/images/editorial/BS_ticker/2017/June17/COMMON-GSE-REFORM-PRINCIPLES-FINAL.pdf.

The Council emphasizes the critical need for enforceable affordable housing goals to ensure increased production of affordable housing across all markets. Although the current affordable housing goals are not adequate, the FHFA's ongoing rulemaking on the goals offers an opportunity for improvement.

QM/QRM

There have been significant policy developments since the Great Recession that have shaped the mortgage market in the United States. There is a need to maintain those sensible protections that have been put in place since the Great Recession. The Consumer Financial Protection Bureau's (CFPB's) QM/QRM rules are an important protection against the securitization of poorly underwritten mortgages, which spread risk through the financial system like a virus.

The CFPB's Ability-to-Repay (ATR) rule provides "safe harbor" treatment for loans that meet certain criteria under the Qualified Mortgage test, and most lenders today only make safe harbor loans, versus "rebuttable presumption" QMs or "non-QMs." While the ATR rule was not meant to limit lenders to originating only QM loans, the perceived legal/regulatory risks lead most lenders to do so. Lenders that originate non-QM loans tend to charge higher rates and fees to offset these risks, leading to many creditworthy (despite not meeting all QM tests) borrowers having difficulty obtaining affordable mortgages. The following adjustments to the QM standard could improve credit availability without jeopardizing consumer protections or increasing credit risk:

- **Increasing the small-loan threshold:** QM loans (currently) cannot include points and fees greater than 3 percent of the loan amount. The exception to this standard is a small loan, for which the current threshold is $102,894, and the low threshold makes it unprofitable for lenders to originate loans slightly-to-moderately above this threshold. Modifying allowable points and fees to a sliding scale would likely increase smaller-balance lending.
- **Revising the definition of allowable points and fees:** The 3 percent limit on points and fees includes fees paid to lender-affiliated settlement service providers, but not to unaffiliated settlement service providers. Similar fee rules for affiliates and unaffiliated entities would increase competition and lower costs.
- **Broadening the ability of lenders to cure for technical errors:** Current QM standards provide insufficient opportunities for lenders to cure or correct errors made in calculating debt-to-income ratios, points, and fees, which creates a lender disincentive to originate loans for borrowers near the QM thresholds. More latitude to correct/cure errors would incentivize lending to more potential borrowers.
- **Expanding the safe harbor:** Currently, loans that otherwise meet the QM standards but which feature an annual percentage rate exceeding the average prime offer rate by more than 150 basis points only receive a rebuttable presumption of compliance—not safe harbor. If this distinction were eliminated, there would likely be an expansion of lending to borrowers who otherwise meet the QM standard.
- **Changing documentation and verification of income and assets:** The CFPB lender guidance on income and asset verification (contained in Appendix Q) does not allow sufficient flexibility for lenders. By permitting alternative underwriting standards, such as those used by the GSEs, the Federal Housing Administration (FHA), and the Department of Veteran's Affairs (VA), the CFPB can foster increased lending to LMI borrowers. Relatedly, the "QM patch" grants QM status to loans eligible for GSE purchase, but is set to expire at the earlier of January 2021 or the date on which the GSEs exit conservatorship. By developing clear criteria to replace the temporary patch with more flexible underwriting standards, the CFPB can improve upon the current lending environment.

The alignment of the Qualified Residential Mortgage standard with the QM standard has helped to provide greater access to financing, and kept open the door for the return of private capital to the mortgage market by streamlining lender compliance and by setting aside the more onerous borrower requirements from the initial proposal, such as large down payments. However, both GSEs mandate (and current QM/QRM rules require) that all mortgage originators use the FICO 04 credit scoring models developed on data from 1995–2000 to determine eligibility for GSE products. These models continue to include paid collections (including medical collections) and exclude rent and utility data. The GSEs use these outdated credit scoring models as factors in setting loan pricing (Loan Level Pricing Adjustors). Credit scoring models developed post-recession have become more predictive of default risk; include rent and utility data; exclude paid collections; exclude judgments and tax liens; and exclude medical past-due payments for the first 180 days. Consequently newer and competitive models are considerably more predictive than the pre-recession models endorsed by QM and QRM.

The Council, echoing advocates nationwide, also urges incentives for lending institutions to couple well-structured lending programs with credit counseling. Quality housing counseling has been shown to limit mortgage default risk and can be enormously valuable to lenders in differentiating and mitigating risk among borrowers with lower range credit scores.[7] There has been limited progress in recognizing this value and incorporating the cost of housing counseling into the mortgage financing structure—likely the most viable way to scale housing counseling services.

Given the scale of poor underwriting and fraud in the mortgage market, there were significant actions by GSEs to "put back" defective loans to mortgage originators and legal action by federal agencies under the False Claims Act. While many of these actions were both necessary and justified, the fear about "putback risk" and False Claims Act litigation were significant factors for many financial institutions in evaluating their participation in mortgage lending and particularly with respect to making FHA loans. The FHA and the Justice Department must complete a process of engagement with industry to arrive at a policy that balances defining safe and fair lending practices with providing industry sufficient clarity about how to avoid unnecessary litigation.

Important investments have been made by the GSEs to provide automated third-party verifications that allow mortgage lenders to sell loans with significantly greater assurance that they will not be subject to "putback risk." There is concern that Congress is not sufficiently resourcing the FHA and Ginnie Mae to effectively carry out their missions, including developing the infrastructure to provide lenders with access to automated verifications, consistent with those efforts at the GSEs. This lack of investment is contributing to lenders—large and small—abandoning their FHA lending.

2. **Trends in Retail Employment:** *Have the communities served by Council members been negatively affected by retail store closures and/or by reduction in retail employment? How have impacted communities reacted to changes in the retail environment? Have you observed any best practices in retail job creation or workforce development in your communities?*

According to Bureau of Labor Statistics, as of August 2017 the retail industry employed 15.8 million people, or roughly 1 in 10 of all jobs in the U.S. economy. However, in 2017 the retail industry has lost nearly 90,000 jobs to date. While this represents a small percentage of the overall workforce, the losses are concentrated in apparel, health and personal care, and general merchandise—all of which disproportionately employ women and workers of color as compared to other sectors of the economy.[8]

[7] See www.freddiemac.com/news/blog/pdf/benefits_of_pre_purchase.pdf; www.neighborworks.org/researchtracking.aspx?id=17892&nid=3c8914c5-fbdb-4e4e-b405-a9cfffc1d236; and www.neighborworks.org/Homes-Finances/Foreclosure/Foreclosure-Counseling/Congressional-Reports.

[8] For changes in employment, see Bureau of Labor Statistics, www.bls.gov/iag/tgs/iag44-45.htm#workforce. For demographics on the retail workforce, see Center for Popular Democracy, "Data Brief: Retail Jobs Today," https://populardemocracy.org/news/publications/data-brief-retail-jobs-today.

California (Los Angeles in particular) has seen the closure of hundreds of retail stores, including apparel, home goods, sports equipment, electronics, and drug stores as well as supermarkets. The disruption has negatively affected first-time workers and minorities, and widespread commercial vacancies have created urban blight. LMI communities are particularly dependent on their local retail economies, and the jobs these businesses have shed are not being replaced. In higher-income communities, specialty retail continues to thrive but employs few from underserved communities.

Low job quality undermines retail sector economic viability. The low wages, poor scheduling, and few career advancement opportunities that traditional retail workers face on a day-to-day basis present significant challenges to the viability of the sector and the stability of the overall economy. Retail overall pays wages slightly below median, but this obscures significant variation across occupations and subsectors. Cashiers are consistently the lowest paid occupation in retail and are disproportionately women of color. E-commerce jobs, such as warehousing and trucking, can be better jobs on average than a salesperson or a cashier in a traditional retail establishment. However, these averages mask wide variation in pay between temporary, contract labor, and in-house employees. There is some evidence that online retailers are increasingly likely to use temporary, contract, or gig labor,[9] thus suppressing wages and job standards that would cover regular employees.

Beyond wages, fair and predictable schedules and access to sufficient work hours are important for economic security and career advancement. Even more than job training, full-time positions are a strong predictor of career advancement in retail. Women of color are disproportionately involuntary part-time workers[10] in retail, which makes it less likely that they will have access to opportunities for promotion as compared to their white, male, full-time counterparts. This is one contributing factor to the lack of women and people of color in upper-management positions.

The relationship between job quality and training and in-store performance is well documented. As MIT Sloan School of Management professor Zeynep Ton has extensively researched,[11] some retailers in highly competitive industries, such as convenience stores, grocery stores, and big box retailers have run successful and profitable businesses by investing in their workforce and providing stable hours, competitive wages, and job training in order to increase productivity and efficiency. Over the last few years, several large retailers, including Walmart,[12] have experimented with improving wages and providing trainings and career pathways for frontline workers in order to increase employee performance and sales. There are also macroeconomic benefits to addressing the quality of retail jobs. According to research by Demos,[13] raising wages, addressing pay equity between men and women, and providing stable schedules in the retail sector alone would lift nearly a half million women above the level of poverty or near poverty, grow GDP by $15 billion, and lead to the creation of over 100,000 more jobs.

Technology is changing the number, location, and quality of retail jobs. Some argue that changes in retail employment signal a structural disruption to the industry, with in-store retail losing ground to e-commerce.[14] E-commerce is projected to continue to grow faster than brick-and-mortar retail. This has several implications for low-income communities and people of color:

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[9] See www.bna.com/amazon-flex-draws-n73014450075/.
[10] See www.nelp.org/blog/data-points-a-look-at-involuntary-part-time-work-in-retail/.
[11] See http://zeynepton.com/.
[12] See www.nytimes.com/2017/08/08/business/walmart-academy-employee-training.html?_r=0.
[13] See www.demos.org/publication/retails-choice-how-raising-wages-and-improving-schedules-women-retail-industry-would-ben.
[14] See www.forbes.com/forbes/welcome/?toURL=https://www.forbes.com/sites/realspin/2017/04/03/how-e-commerce-is-raising-pay-and-creating-jobs-around-the-country/&refURL=&referrer=%20-%206533f8616dff.

- **Low job growth:** The number of jobs created through e-commerce is unlikely to replace jobs lost in brick-and-mortar stores; department stores have lost 448,000 jobs during the last 15 years, while e-commerce has gained 178,000 jobs.[15] Analysis of business sales shows online retailer Amazon generated $1.5 million in sales for every full-time warehouse worker it employed in the state of Illinois, while brick-and-mortar retailers employ about seven people to generate the same level of sales.[16]
- **Geographic concentration of jobs:** The change in geography of new jobs in online retail is likely to leave many communities behind. Brick-and-mortar retail stores are fairly evenly distributed across the country.[17] In contrast, jobs in e-commerce are increasingly concentrated in a smaller number of areas. Amazon, which captures 43 percent of all online retail sales, delivers to every state yet does not have a physical presence in 16 states.[18] Fulfillment centers and warehouses have shifted in recent years to the fringe of major metro regions as demand for same-day delivery has grown. Many of these new facilities are located in areas with little or no affordable housing for the workers they will employ, leading to long commutes in areas that often lack public transportation.
- **Reach of automation to low-wage and entry-level jobs:** Job automation for truckers, warehouse workers, cashiers, and retail salespeople will disrupt these jobs in ways that are difficult to predict. In some retail stores, technology is aiding workers to increase productivity and efficiency, such as taking inventory, counting out registers, or fulfilling orders. There is also potential that automation will eliminate many jobs.[19] However, considering the capital investment necessary for automation, many retailers are seeking to reduce costs by shifting to a contingent workforce and just-in-time scheduling, which could erode job quality.

According to retail-worker advocacy organization OUR Walmart, policy responses to mitigate the impact of tech-driven job changes have been slow to materialize. Job losses in areas like mining, which is predominately white and male, have received significant political attention, while the predominantly female and of-color retail workforce has received relatively little attention.[20] This is not an either/or issue since the loss of retail jobs and retail store closures hit first and hardest in rural regions—including coal communities.

There is some evidence that recent job losses in retail have additional contributing factors aside from technological changes. According to data gathered by the Center for Popular Democracy, the heavy debt loads associated with the approach by some private equity firms seem to be playing a role in the recent growth in retail bankruptcies and related store closures and jobs losses.[21] Private equity firms owned nearly half of the retail and grocery chains that have filed for bankruptcy since 2015.

[15] See www.nytimes.com/interactive/2017/07/06/business/ecommerce-retail-jobs.html?mcubz=0.

[16] Olivia LaVecchia and Stacy Mitchell, Amazon's Stranglehold: How the Company's Tightening Grip Is Stifling Competition, Eroding Jobs, and Threatening Communities (Washington, DC: Institute for Local Self-Reliance, November 2016), https://ilsr.org/amazon-stranglehold/.

[17] However, evidence from the Center for Popular Democracy shows that recent store closures are unevenly concentrated in LMI suburbs that are struggling economically; see www.bloomberg.com/view/articles/2017-01-13/your-local-mall-is-dying-unless-you-are-rich.

[18] See www.businessinsider.com/amazon-accounts-for-43-of-us-online-retail-sales-2017-2. Amazon does not have a physical presence in Alaska, Arkansas, Hawaii, Idaho, Iowa, Louisiana, Maine, Mississippi, Montana, Nebraska, New Mexico, North Dakota, Rhode Island, South Dakota, Vermont, and West Virginia.

[19] See www.bloomberg.com/graphics/2017-job-risk/.

[20] See www.theatlantic.com/business/archive/2017/04/the-silent-crisis-of-retail-employment/523428/.

[21] See www.wsj.com/articles/vendors-landlords-target-private-equity-firms-in-retail-rubble-1501412401?mod=pls_whats_news_us_business_f.

Local retailers face additional pressures in today's climate of policy uncertainty, stemming in part from the unpredictability of the current administration, related to trade, tariffs, and import duties. They also include more targeted policies on tariffs and import duties that are driven by congressional actions such as the Generalized System of Preferences Program. In the same vein, these businesses may be more important in current context as retail access is easier for most through e-commerce, but more difficult for those in marginalized markets. Also, gentrification can affect traditional local businesses in much the same way it does residents.

There are a number of positive trends in the retail marketplace that are worth encouraging, however:

- Local small retailers contribute significantly in places that may lack access to e-commerce or big box options. These local retailers stabilize and increase the vibrancy of urban corridors in neighborhoods, provide realistic entrepreneurship opportunities, and create jobs for local residents. In communities such as Detroit, Cincinnati, and New Orleans, there are aggressive measures to provide the capital, address real estate barriers, and/or bundle resources to grow local retailers. New Orleans has created training programs to give at-risk youth the needed skills to move into the retail and hospitality sectors, largely due to the recognition of the lower barriers to job entry and traditionally clear paths to promotion and income growth.
- The federal government's Healthy Food Financing Initiative (HFFI) has demonstrated that there are solutions to the food-desert problem. Since 2011, this program has provided $220 million in federal investments that has, in turn, attracted more than $1 billion in private investments. It has helped create or support nearly 1,000 grocery stores and other healthy food businesses in 35 states and has supported 100 community development organizations. However, challenges remain in terms of reaching more rural communities, for example where the loss of a grocery store can be devastating to the community.
- Technology has, among its many impacts, brought much more transparency to sourcing and supply chains, allowing retailers and their consumers to understand how the money they spend impacts the people and places that are connected to those supply chains. Fair trade and buy local movements are more active and effective than ever, and the consumer demand for the information they provide continues to grow. While mega-stores create concern, there are positive examples of very large retailers actively creating space for small retailers and slightly altering their product mix in a given store in order to allow small businesses to thrive. These sorts of partnerships provide many consumers with a more diverse and satisfying shopping experience while allowing large companies to more effectively integrate with local economies, rather than simply representing an outflow of capital.
- The retail market in Massachusetts hasn't been as significantly affected by the downturn as other parts of the country. Grocery stores (the introduction of Wegmans and Price Chopper), as well as the introduction of some big box stores like Primark, have driven this trend. And Massachusetts' minimum wage of $11 per hour has not seemed to slow retail employment, particularly in eastern areas of the state. In fact, Boston and Cambridge ranked 1 and 2 in the list of top 10 towns by retail square footage.[22] This provides greater opportunities for LMI job seekers to enter the labor market in the Greater Boston area. Similarly, New Hampshire has experienced a slight decrease in vacancy rate from 10.5 percent in 2016 to 9.1 percent in 2017.[23]

3. **Labor Markets:** *How have the labor markets in which Council members operate changed since the May 2017 meeting? In particular, assess the degree of job loss or gain (how much and in which industries). What changes to wages for LMI earners have Council members observed?*

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[22] See www.keypointpartners1.com/MarketReports/EaMA2017.pdf.
[23] See www.keypointpartners1.com/MarketReports/SoNH2017.pdf.

In July 2017, Prosperity Now issued the *2017 Prosperity Now Scorecard,* which provides both outcome measures and policy recommendations to build and protect the financial security and opportunity of U.S. households and includes data on the impact of the changing labor markets on households and consumers. The data indicate that despite the drop in unemployment, there has not been an increase in the number of quality jobs—those that pay enough to cover expenses and enable workers to save for the future. The 2017 Scorecard reports that one in four jobs in the U.S. is in a low-wage occupation, which means that at the median salary, these jobs pay below the poverty threshold for a family of four. The rate of low-wage jobs has remained relatively stagnant since 2012, and in six states (Alabama, Arkansas, Louisiana, Mississippi, New Mexico, and West Virginia), more than one in three jobs is in a low-wage occupation. For the first time, the 2017 Scorecard includes a measure of income volatility that shows that one in five households has significant income fluctuations from month to month. The percentage varies by state, from a low of 14.7 percent of households in Virginia to a stunning 29.8 percent of households in Wyoming. In addition, 40 percent of those experiencing volatility reported struggling to pay their bills at least once in the last year because of these income fluctuations. These two factors contribute significantly to the fact that almost 37 percent of U.S. households, and 51 percent of households of color, live in the financial red zone of "liquid asset poverty." This means that they do not have enough liquid savings to replace income at the poverty level for three months if their main source of income is disrupted, such as from job loss or illness. This level of financial insecurity has profound implications for the security of households, and for the overall economic growth of the nation.

Wage and worker protections. Across the country, the debate over a higher minimum wage continues as a primary strategy to improve the quality of jobs. Some cities and states have approved legislation to phase-in a minimum wage increase to $15 per hour over time, while others have rescinded earlier legislation supporting those increases. The data is supporting that the major impact of these ordinances is on large franchised businesses and retail chains. In addition, access to physical and mental health services for workers is essential to both job performance and tenure.

LMI communities also face other barriers. For example, wage theft and health and safety violations continue to be issues in Massachusetts. The state attorney general's office is going after employers who are not paying overtime or not paying their workers at all (particularly undocumented workers). In addition, farmworkers in particular continue to face some of the most challenging labor conditions due to their exemption from most labor standards, minimum wage requirements, and many health and safety protections. Farmworkers deserve a national minimum wage standard and safe working conditions.

Immigration policies. The current uncertainty surrounding the Deferred Action for Childhood Arrivals (DACA) policy is creating a great deal of instability in labor markets by throwing the lives of 800,000 Dreamers—children and their families—into fear and disarray. This fear inhibits economic activity such as small business growth, access to education and training opportunities, and job applications. The elimination of DACA is projected to reduce GDP by $460.3 billion and Social Security and Medicare tax contributions by $24.6 billion.[24] 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.

[24] See www.americanprogress.org/issues/immigration/news/2017/08/28/437956/daca-recipients-economic-educational-gains-continue-grow/.

Disparities by race and disability. Barriers to economic stability disproportionately impact people of color and disabled workers, who continue to struggle despite employment gains across the broader workforce. While national labor statistics suggest that the economy has reached full employment, for blacks the unemployment rate is at 7.7 percent. The unemployment rate for persons with a disability was 10.5 percent in 2016, about twice that of those with no disability.

The racial disparities are especially significant in the southeastern region of the country, where unemployment rates are generally higher for people of color. Qualitative evidence from focus groups in the southeastern region reveals the following key themes:

- Burdensome childcare costs present a barrier to work as childcare costs, along with the constraints of normal work hours, make it difficult to find work that can accommodate working parents—a problem not solved by the childcare voucher system.
- Limited transportation options constrain access to employment. This is especially prevalent in the Atlanta metro area due to restrictive schedules and route limitations of public transit.
- Elder care responsibilities hamper the ability of some people to work during prime earning years.
- "At will" employment laws allow arbitrary firings, and discriminatory hiring practices are common.
- Criminal records are a significant barrier even when the public sector has made attempts at ban-the-box policies where private sector has not adopted these policies. There is significant innovation under way in the nonprofit and public sectors to reduce financial and legal barriers for "returning citizens," including implementing public policies to restore Pell Grants for those with criminal records and sectors, such as manufacturing, that welcome re-entry employees.

People with disabilities face ongoing barriers to employment created by rules governing asset limits, accessible workplace policies and labor standards, and reliance on "sheltered workshops," which are allowed to pay subminimum wages. In contrast, advances in assistive technologies are transforming opportunities for people with disabilities to successfully work in competitive employment.

Disparities by regions and sectors. Employment rates are rising in several regions, including the Midwest, New England, and several western states. This trend is creating financial gains for LMI workers while creating employment challenges in sectors such as childcare. While nonprofit childcare centers represent a lifeline for LMI families, these centers are experiencing what we refer to as a "workforce crisis" because they are unable to compete for workers in an improving economy.

Construction workers, with a few exceptions, are also seeing increases in demand and pay, with recent contracts gaining wage and benefit increases around 3 percent a year. One of the most notable exceptions is heavy construction, which relies on funding infrastructure projects which have not received the investments that are necessary. Manufacturing has continued to have mixed employment results. Defense contractors and other manufacturers have slowly increased hiring, while GM and Harley-Davidson have had to lay off workers and scale back hours. Railroad workers are suffering the biggest losses.

There have been shifts in energy markets and subsequent job losses in coal and power plants in key regions that are also driving multiple effects on local labor markets. This means energy-market-impacted communities are not only struggling to recreate economies hurt by the mono-economics of coal, but have also lost many of their retail jobs. However, there is a growing interest in locally grown, produced, and sold goods and services, which is slowly creating new jobs that could be promising for rural and small neighborhood businesses.

4. **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?*

Recent congressional action to overturn the CFPB's rule on forced arbitration is a profoundly negative development in the U.S. marketplace. The CFPB rule prohibits consumer contracts from denying Americans the right to band together in a lawsuit against a company for misconduct. Forced arbitration makes it very difficult for average Americans to hold companies accountable when they engage in abusive conduct, distorting private market incentives for companies to meet consumer needs.

Rural Communities

In many rural places, like Appalachia, markets are broken. Traditional means of financing housing and small businesses do not work, particularly in places where infrastructure like buildings, water systems, and sewer systems are dilapidated. In some areas, credit unions, Community Housing Development Organizations, community development corporations, and Community Development Financial Institution (CDFIs) provide relevant capital and services in these communities, but existing subsidies are not adequate to have the impact needed to jumpstart new markets. Public and private investments must be aggregated to build local and regional community development capacity.

Small Business Lending

There is a pressing need for more data on small business lending in the United States, and the CFPB should implement section 1071 of the Dodd-Frank Act to collect data from banks on their small business lending. There continues to be significant differences in what type of credit, or loan, is available to men and women, minorities and nonminorities, urban versus rural, and underserved and well-served communities. Differences are manifested in loan terms: interest rate, length of amortization, fees, and availability. Small Business Administration (SBA) lending to women and minorities continues to be disproportionately low relative to their representation in the population. According to a 2016 Stanford Graduate School of Business national study, in 2015, 27 percent of Latino small business had never heard of the SBA, and 71 percent had never heard of SBA Small Business Investment Companies (a growing vehicle for commercial bank equity investments into small business).

Over the past year, NALCAB – National Association for Latino Community Asset Builders has released research on Latino small business in state and local markets around the country. Its key findings include that

- Latino-owned businesses operate in diverse industries and markets;
- Latino-owned businesses represent an enormous growth market for small business lenders and a key driver of economic growth, especially in states like California and Texas;
- Latino-owned businesses have, on average, less annual revenue and staff than non-businesses and distinct credit/collateral profiles to which, given the growth potential, lenders should adapt their underwriting; and
- CDFIs play a critical role in opening access to capital for Hispanic-owned small businesses and act as a bridge to larger financial institutions.

Although banks seem more willing to make credit available to borrowers with less than stellar credit, they are not willing or able to analyze credit in a safe but creative manner. Often borrowers are forced to seek merchant cash advance loans, which are based on a business's credit card processing and corresponding gross cash flow and ignore the business's ability to repay loans. Merchant cash advances typically have higher rates and shorter amortization and choke off desperately needed cash flow. The Council sees low-income people of color and immigrants (who do not qualify for traditional credit or choose not to use it) being particularly hurt by this industry. There is also a shortage of Sharia-compliant financing, which impacts Muslim business owners.

Several jurisdictions in the South are working to advance economic inclusion strategies, including anchor institution engagement, minority-owned business development, and targeted workforce and hiring strategies. There is a need to develop the capacity of small and minority-owned businesses, particularly black-owned businesses, to attract new capital and to increase the availability of capital for these businesses.[25] Lack of loan funds available for local CDFIs is a significant challenge. Leveraging Community Reinvestment Act requirements to encourage financial institutions to make equity-equivalent investments, loans, and loan-loss reserve grants to local CDFIs will help alleviate this challenge. A new report from Prosperity Now confirms that black entrepreneurs in the South are challenged by "limited startup capital, limited managerial and industry experience, and lower-revenue industries, i.e. retail."[26]

Home Mortgages

Credit issues continue to be the primary reason that first-time homebuyers are unable to qualify for mortgages. The markets are having challenges accessing liquidity via the capital markets as a result of tight credit criteria that otherwise could be adjusted to support sustainable homeownership. In a recent Loan Denial Pilot program, a small cohort of lenders in Minnesota examined the files of borrowers whose applications had been denied in an attempt to better understand where resources can be applied to improve creditworthiness. This pilot program review confirmed that credit issues continue to be the primary problem and that 75 percent of those with credit issues were households of color. It appears that longer periods of more intense financial coaching for households is an increasingly important element for those that have the financial capacity and the desire to become homeowners.

There has been a substantial uptick in mortgage credit access for residents of Detroit. Historically, undervalued and older buildings, vis-à-vis other options in the region, inhibited the ability of financial institutions to offer a product that was accessible and affordable. These challenges were further exacerbated by issues such as a lack of sales comparisons (for underwriting purposes) and depressed insurance valuations. Currently, home values across the city have not yet fully recovered from the recession. In 2014, approximately 10 percent of the 4,000 completed home sales were financed, as most banks recognized the value at less than 80 percent of the actual sales price. The Detroit Home Mortgage partnership led by the Community Reinvestment Fund, the Kresge Foundation, the Ford Foundation, the City of Detroit, the Michigan State Housing Development Authority, and several banks launched a tailored mortgage program, Detroit Home Mortgage, in late 2016 that allows people to borrow up to $75,000 more than the home's current appraised value. This seems to be having a significant impact on mortgage access in the city and is evidence of a successful local effort when communities unite to provide a solution.

[25] Evidence gathered from PolicyLink listening sessions in the summer of 2017 with city staff and community leaders in all seven cities—Asheville, NC; Atlanta, GA; Charlotte, NC; Memphis, TN; Nashville, TN; New Orleans, LA; and Richmond, VA –– about challenges and themes in their cities.

[26] See https://prosperitynow.org/files/PDFs/07-2017_stuck_from_the_start.pdf.

Multifamily and Affordable Housing

Hot residential (and commercial) markets (i.e., high land costs/speculation) are making development and financing of affordable housing and affordable commercial space difficult. Income is not keeping pace with the rise in costs of residential and commercial space.

Consumer Lending

Consumer loans can be a dangerous trap for borrowers, particularly those with few assets. For example, home improvement loans are often not available to LMI homeowners, forcing these borrowers to seek high-interest loans that are often predatory. Furthermore, the ability to access home improvement loans is often impossible where home values have not recovered or in rural areas where property continues to depreciate rather than appreciate.

The same kinds of investors that invested in institutions providing predatory subprime mortgage products prior to the foreclosure crisis have invested heavily in auto-title loan portfolios. Similar to the foreclosure crisis, record numbers of people are having their cars seized for nonpayment. Consumers already have $1 trillion in credit card debt and $1.4 trillion in student debt, close to levels before the Great Recession, and once again, people of color and low-income people stand to be hardest hit.

Regulation plays a key role in ensuring that LMI consumers are protected. The CFPB has finalized a key payday lending regulation, but Congress may attempt to repeal it. The bureau has also proposed regulations for many other important financial markets and services that could potentially face repeal, including overdraft protections and regulations for debt collection.

Recent emergence of unregulated financial institutions is also harming vulnerable consumers. One flawed business model, the so-called “finder” or “referral partner” business model, encourages customers to take out a small-dollar loan that is referred by an unregulated third party who is compensated for that referral by the lender. In 2017, the California Department of Business Oversight reported that the majority of finders are payday lenders, car title lenders, or high-cost check cashing agencies. Unfortunately, the majority of borrowers receiving loans through a finder saw their credit scores go down. Other examples of unregulated financial activities include online payday loan brokers selling personal financial information to third parties without borrowers’ knowledge and the proliferation of Property Assessed Clean Energy financing (PACE loans), where unregulated private contractors solicit new borrowers by canvassing neighborhoods door-to-door without proper disclosures. Alternatives to high-cost lending must be scaled for people with little or no credit history.

5. **Housing Markets:** *How have house prices and rental rates changed since the May 2017 meeting? Have there been any new developments in housing activity for LMI communities in Council members’ regions?*

Many parts of the country are experiencing great impediments to the availability of affordable housing for LMI communities. A recent analysis by PolicyLink and the USC Program for Environmental and Regional Equity looked at the growth of renters, their contributions to the economy, and what renters and the nation stand to gain from more affordable housing. The analysis found that renters now represent the majority in the nation’s 100 largest cities and are growing as a share of the population nationwide. Renters make tremendous contributions to economic, social, and political life. They represent $1.5 trillion in consumption per year (excluding rent and utilities). Yet across America, renters face a troubling mix of rising rents and stagnant wages, both of which add up to an unprecedented affordability crisis. The portion of households paying more than 30 percent of their income on rent and utilities has increased from 39 percent of households in 2000 to 51 percent in 2016. LMI renters, particularly people of color and women, are squeezed by the rent crisis and stand to gain the most from lower rents and higher wages.

Rental vacancy rates are the lowest ever in the U.S. at 2.6 percent and 2.7 percent, respectively, for the first and second quarters of 2017. Additionally, rents are increasing throughout the country. For example, across the state of California, rent has increased almost 10 percent over the last year, pushing LMI individuals into making tough decisions about where to live, eat, go to school, and work. The neighborhoods that are affordable to LMI households are on the outer edges of the region and are considered "low-opportunity" neighborhoods according to the Child Opportunity Index, a comprehensive analysis of opportunity in neighborhoods created by DiversityDataKids.org and the Kirwan Institute for the Study of Race and Ethnicity. A lack of affordability is pushing LMI communities toward the outer edges of the region and is widening racial inequality. These conditions take a tremendous toll on families and employers. Employers have a hard time recruiting and retaining employees who cannot afford to live within a reasonable distance, particularly if public transit is scarce or nonexistent.[27] The shortage of affordable housing is particularly acute in the Bay Area. Rental data from Zillow and other sources shows that while 41 percent of full-time workers in the five-county Bay Area region earn less than $25/hour, less than 1 percent of rental units are affordable to those workers (i.e., they are paying more than 30 percent of their income on rent and utilities). The data also show that for a family of two workers earning $15/hour, only 1 percent of neighborhoods are affordable. In fact, 90 percent of neighborhoods are only affordable to households with an annual income at least $100,000.

Over the past two years, NALCAB has studied the dynamics of changing neighborhoods in multiple urban markets and documented the impacts of increasing real estate values on the integrity and survival of long-established, LMI communities of color. Large-scale public investments in infrastructure, parks, stadiums, and housing often drive private investment into areas that previously experienced little or no investment. While these major public investments often improve and strengthen neighborhoods, without concurrent investments to maintain affordability, low-income residents are often displaced due to rising real estate values (and taxes). San Antonio's Mayor recently established a Housing Task Force to undertake a public and data-driven review of the city's housing policy as well as impacts of neighborhood change on vulnerable populations.

In rural communities, rental and subsidized housing also face a number of challenges. Many of these housing units were developed almost 20 years ago with flexible Housing and Urban Development and U.S. Department of Agriculture rural development financing that allowed for varied rent and income limits. Now these projects are aging out, have deferred maintenance, and can't support themselves with the current rent/income limits. These properties—many of which have loans nearing maturity—will be difficult to refinance without significantly raising rents, an act that would likely make them unaffordable for many current residents.

For the first time since the Great Recession, homeownership has gone up. However, this may not translate into improvements in ownership for families of color and LMI. Exploring regional and local housing trends would help explain what is happening here. In many markets, building housing for LMI residents is not as profitable, and therefore, it is not being built at a scale that matches demand and need. This has created a very competitive market for rental housing—detrimentally impacting those who can least afford it. LMI homeowners are also impacted by rapid appreciation as a result of increases in property taxes, insurance, and other housing-related costs. For example, in Rhode Island there is a shortage of affordable homes, with the inventory for homes priced below $200,000 at 1.36 months, and for homes priced between $200,000and $300,000, at two months. For six years, Rhode Island has placed last in the nation for building-permit activity. Not surprisingly, home prices are rising, with the June median price hitting $275,000—the highest since the pre-recession peak. A shortage of construction workers stemming from heavy job losses during the recession and an aging workforce have compounded this problem. The Rhode

[27] See www.propertyradar.com/blog/san-francisco-bay-area-challenging-housing-market-a-factor-in-the-region-employment-growth-slowdown.

Island Builders Association is using some of the governor's economic development tools to train young people coming out of technical schools to enter the construction trades, especially in those occupations in high demand by builders.

The middle of the country has not been immune to affordable housing shortages either. For example, housing markets continue to be very tight in Minnesota, with low vacancy rates and rising rents in multifamily housing and shrinking inventories and rising prices for single-family homes. The inventory of existing single-family homes priced under $250,000 is particularly tight, with only a 1.5 month's supply in June of 2017. The median sale price for single-family homes in the Twin Cities metro area is up 2.0 percent since May from $250,000 to $255,000, and new listings are down by 3.6 percent over the same period. There continues to be little or no new construction for homes below $250,000, as developers focus on building rental apartments rather than condominiums and townhomes. Home builders indicate that the high price of land and the cost of regulatory conditions make it nearly impossible to produce affordable detached homes for moderate income buyers.

Moving on to South Florida, the shortage of housing is equally acute among both rental and for-sale homes (single-family and multifamily). The key barrier to greater home ownership is not the credit markets or the credit worthiness of potential borrowers. Rather, it is the low inventory of homes for sale and the increasing prices.

Homelessness is a critical issue that is directly related to the affordable housing crisis. Family, child, and individual homelessness continues to be a challenge in some markets across the country. There are myriad contributing factors driving this challenge. These factors include lack of housing affordability; unemployment or underemployment; bills are higher than what the household can afford; mental health issues; domestic violence; and evictions, among others. But the main reason that LMI people experience homelessness is because they cannot find housing that is affordable. It is important to further review and examine the complexities of homelessness in light of the affordable housing crisis in this country, which is compounded by mental health and substance abuse issues that are on the increase.

In summary, while certain market conditions are considered to be favorable for the development of additional affordable housing units and homes (e.g., lower interest rates, increases in the use of Private Activity tax-exempt bonds), the production has not kept pace as the cost of production (i.e., acquisition, labor, and materials cost) continues to increase. However, federal tax reform proposals, released on November 2, to eliminate private activity bonds would eliminate resources available for affordable rental housing developed with 4 percent housing tax credits, creating a major impact especially in high-cost areas. Elimination of these bonds will also reduce the availability of financing for first-time home buyers.

6. **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?*

On September 20, 2017, Puerto Rico was hit by the disastrous Category 4 Hurricane María. The path of this terrible storm left 3.4 million American citizens living without power, clean water, food, basic services, medical care, and, in many cases, without homes. It is estimated that the hurricane destruction will amount to up to $95 billion—a devastating blow to the island's already ailing economy—where the GDP is $103 billion. Before María, and before that, Hurricane Irma, 45 percent of the island's residents lived in poverty and unemployment hovered between 12 percent and 14 percent. Puerto Rico was in the midst of a harmful economic and humanitarian crisis that had weakened its infrastructure, its labor and housing markets, and its health care and education systems and had that decimated its population.

Before the devastation left behind by the hurricanes and due to the U.S. financial crisis, Puerto Rico's population had declined by 7 percent from 2010 to 2015.[28] Given the current calamitous situation, many Puerto Ricans are leaving the island at dramatic rates, and it is estimated that over 100,000 people will leave within the next year as they seek to survive the exacerbated crisis. This is problematic as a further drop in the population would make it harder for the island to rise from its economic abyss. Puerto Rico declared bankruptcy in May 2017 and has stopped making payments on much of its $73 billion debt. A massive exodus would mean less economic activity and further reduce much-needed tax revenue for the island, which in turn would further reduce the island's ability to repay its debt.

Puerto Rico is not alone in its disaster recovery efforts. The destruction caused by hurricanes through the southeast, Texas, and the U.S. Virgin Islands as well as by the fires in California place tremendous pressure on communities as they seek to rebuild.

The recovery efforts in these disaster areas, while urgent, do not begin to address the complex, longer-term systemic issues in these same communities as well as in other LMI communities. In short, solutions are needed to change the trajectory of two lines: the steep upward line associated with rising housing costs and the lower, stagnate line representing the wages of American workers. The distance between these two lines is captured by ongoing research and the growing income and wealth disparity between white and minority households.[29] These gaps, evident in national statistics, along with the lack of American economic mobility, must be addressed with a set a measures tailored to the unique characteristics of each community.

Labor markets and housing markets differ across our country, so sustaining solutions to create and uplift markets are best designed through interactions among community leaders, business leaders, and the financial community. Together, these stakeholders can craft and prioritize incentives that recognize the complex intersection of various labor issues (e.g., returning citizens, mental health, immigration, and workforce development), infrastructure (e.g., affordable housing, transportation, power grids), climate change (e.g., zoning, rebuilding in flood zones, and mobile home parks in hurricane areas). Ideally, community affairs offices throughout the Federal Reserve System can develop a repository of successful case studies and convene, as a part of its CRA initiatives, catalytic discussions on how communities can develop best practices to solve these challenges.

To help inform this conversation, the Council would appreciate an opportunity to shed insight on some of the more complex issues facing communities, including transportation, the opioid crisis, climate change, and homelessness. Collectively, we seek to highlight the intersection of these issues on traditional measures of economic success.

[28] See www.pewresearch.org/fact-tank/2016/03/24/historic-population-losses-continue-across-puerto-rico/.

[29] The research showed that if wealth trends continue to unfold as they have over the past 30 years, then (1) by 2020, Latino and black median wealth is projected to decrease by about 10 percent and 20 percent, respectively, and (2) by 2024, Latino and black wealth is projected to decrease another 20 percent and 30 percent, respectively. The study also found that black and Latino median wealth is projected to reach zero by 2053 and 2073, respectively.