Community Reinvestment Act Joint Public Hearings, August 12, 2010
Panel Two: Eugene Ludwig

Eugene Ludwig:
I want to thank the Federal Reserve of Chicago for hosting this hearing to discuss the Community Reinvestment Act and I want to commend all our federal bank regulators for their leadership in undertaking this endeavor to consider enhancements that will advance the cause of equitable credit availability, promote sound lending practices and otherwise ensure the availability of banking services to underserved communities. I'm deeply honored to be here. I have a tremendous amount of respect for our federal officials who are conducting this hearing today.

More than 33 years have passed since the CRA become law and in that time it has done and great and measurable good. At the same time, since its passage and particularly in the past three years, we've witnessed extraordinary changes in finance. The task today is a worthy one: to examine how the CRA can contribute most effectively to shaping a stronger but equitable financial system. Although the CRA has been the law for decades it has always attracted its fair share of debate. Bankers have sometimes criticized the CRA as unnecessary and burdensome, particularly the small banks. That criticism was more prevalent before the Clinton Administration's 1994 regulatory reforms of the CRA, which is a controller I was honored to be part of. We accomplished the changes, I think, which were needed at the time by eliminating unnecessary burdens on banks and by assessing actual performance. I might add that the credit made available to low and moderate income Americans through CRA programs during this era was not only transforming for low and moderate income communities but it was almost without exception, profitable and safe.

Unfortunately, the CRA is not keeping up with innovations and trends in the financial industry, most notably industry consolidation and non-depository lending, and this is eroding the acts of effectiveness. The financial services business and the matter in which financial products are structured, offered, delivered and held by institutions and investors has fundamentally changed since 1977. At the time Congress was debating the CRA back then, banks were the dominant financial services companies and were the dominant debt holders. Banking was still largely a local matter; trillion dollar coast to coast banking operations were on the very distant horizon and not the reality.

Over the last 35 years however the banking and thrift industries have been losing ground to the other financial services companies as has community banking. The result is that non-bank lenders now hold more credit market assets than do banks and thrifts, and the largest banking organizations in America worth the community banking sector. Vigorous application of the CRA is as necessary now as it was in 1977. In order to ensure that there continues to be a flow of investment on fair terms to LMI neighborhoods, reigning in the excesses of subprime lending may have a disproportionate impact on LMI areas, especially if lenders and investors take away the wrong lesson from the experience: that LMI borrowers are not good credit risks, which is certainly not the case. Indeed, inner cities and economically declining regions require large capital investments and infrastructure and the demolition or rehabilitation of dilapidated properties if they are to be attractive environments for private capital investment.

How then do we reconcile providing credit to the underserved while at the same time protecting consumers in the economy? I recommend the following: 1. Apply the obligation to meet the needs of LMI neighborhoods and communities to non-bank financial services companies. Their share of financial assets now exceeds those of banks and thrifts and their holdings continue to grow. The Federal Reserve is in essence open to supporting almost all large financial services companies regardless of charter in the storm, broker dealers, insurance companies and credit unions should be covered by the CRA at a minimum. Ideally, the CRA would also apply to all over major financial institutions important to the maintenance of a stable economy, such as hedge funds and private equity funds of any entity that has over 250 million in assets consistent with [inaudible] Gram-Leach-Wiley small bank cutoff. 2. The holding company structure allows banks to reduce their CRA obligations by pushing activities out of the bank into the holding company affiliates; and this has been going on for awhile and is common in the mortgage and consumer lending areas. This anomaly needs to be rectified. 3. In many cases the area served by a bank is no longer self-evident or defined by a geographic community. Virtually all the top 50 banking companies have extensive interstate banking operations. Anchoring CRA obligations to the LMI area surrounding a charter or headquarters location, does not often reflect the reality of their businesses or their impact on LMI consumers.

I think I'm out of time. I have the rest of my testimony with the additional recommendations which I've submitted for the record so if the panel is okay I'll then stop there.

Elizabeth Duke:

Okay thank you.