

N A A H L

NATIONAL ASSOCIATION OF AFFORDABLE HOUSING LENDERS

CRA DID NOT CONTRIBUTE TO THE MORTGAGE CRISIS

WHAT IS CRA?

Congress enacted the Community Reinvestment Act (CRA) in 1977 to encourage insured depository institutions to help meet the credit needs of their communities. Over the past 30 years, banks and not-for-profit lenders have worked hard to increase the flow of private capital to underserved areas. The law has helped to revitalize our nation's low- and moderate-income (LMI) communities by increasing access to credit, on **fair terms**, and in a **safe and sound manner**. CRA has fostered public-private partnerships that leverage scarce government subsidies with a multiplier of private capital.

"CRA projects also act as catalysts for other investments, job creation, and housing development. Such infusion of capital into these markets leverages public subsidies, perhaps as much as 10 to 25 times, by attracting additional private capital. Many of these CRA equity investments can be made under national banks' public welfare investment authority." - Former Comptroller of Currency John Duganⁱ

THE ALLEGATION

In recent years, CRA has come under attack for supposedly weakening lending standards and fueling the subprime mortgage crisis.

THE TRUTH

CRA did not contribute to the mortgage crisis – in fact, it did the opposite, promoting responsible lending in a time when doing so was outside of the norm.

THE PROOF

The vast majority of loans that drove the mortgage crisis did not count toward CRA credit

89% of all mortgages made between 2004 and 2006, the peak of the subprime boom, did not count toward CRA credit, according to the Center for Community Capital at the University of North Carolina, Chapel Hillⁱⁱ.

According to the Federal Reserve, approximately 94% of higher-priced loans were made by companies not covered by the CRA at all or outside of CRA assessment areasⁱⁱⁱ.



“...the very small share of all higher-priced loan originations that can reasonably be attributed to the CRA makes it hard to imagine how this law could have contributed in any meaningful way to the current subprime crisis.” – Former Federal Reserve Governor Randall S. Kroszner, in a 2008 speech

CRA loans are safer than other types of loans

CRA loans are on the whole profitable and not particularly risky, a Federal Reserve study found^{iv}.

Furthermore, economists at the Federal Reserve Bank of San Francisco found that even when controlling for a borrower’s income level and other risk factors, CRA loans performed better than loans originated by institutions not covered by CRA. Loans originated by independent mortgage companies were twice as likely to be in default or foreclosure^v. UNC-Chapel Hill’s Center for Community Capital came to similar conclusions and also found that CRA loans were less likely to include predatory characteristics like high interest rates and prepayment penalties: **“All CRA-regulated institutions are statutorily required to comply with 'safe and sound lending practices'”**^{vi}.

Overall, CRA promotes safe and responsible lending in LMI communities. Harvard’s Joint Center for Housing Studies found that most prime loans in LMI neighborhoods are originated by CRA institutions^{vii}. It is therefore unfortunate (and telling) that the majority of LMI lending was not covered by the CRA during the housing boom^{viii}.

“If the Community Reinvestment Act caused the subprime crisis, it is hard to make sense of why non-covered lenders drove the growth. These subprime lenders were competing with more responsible lending under [CRA] by banks and thrifts. Their loans undid the work of community banks that had been making sound mortgage loans to creditworthy borrowers for years.” – Treasury official Gene Sperling and former Treasury official Michael Barr, now a University of Michigan Law Professor, in a New York Times opinion piece^{ix}

Lending to LMI populations is not inherently dangerous – it is how you lend that matters

The San Francisco Fed study not only shows that CRA loans are safe, but also makes a broader point about lending in LMI communities: its inherent risk is overblown, and what risk factors there are can be substantially mitigated by prudent or regulated business practices. A study by UNC’s Center for Community Capital showed that borrowers sharing similar characteristics had different rates of default depending on the type of loan products they purchased – CRA loans, less likely to have high interest rates or other risk factors, performed better^x. **Sadly, more than half of the borrowers who took out subprime loans could have qualified for prime loans** (as the vast majority of CRA loans are), the Wall Street Journal reported^{xi}.

Additionally, a study published by the St. Louis Federal Reserve found that slightly more than half of all subprime loans were refinances^{xii}.



CRA's influence was waning, not expanding, in the year's leading up to the crisis

Banks and thrifts have been subject to CRA since 1977. The boom in loans that drove the foreclosure crisis occurred from 2001-2006, a period in which CRA's influence was at an all-time low. The share of home mortgage debt held by CRA institutions had plummeted since the law's enactment: from 73.9% when the law was created in 1977, to 32.7% when it was amended in 1995, and to 26.4% in 2008^{xiii}.

By the height of the subprime boom, the majority of LMI lending was not covered by CRA. "Shadow" banking by unregulated independent mortgage companies proliferated^{xiv}.

THE VERDICT

The claim that CRA fueled the mortgage crisis just doesn't add up – CRA loans were safe and CRA incentives encouraged more prudent lending. In fact, the aforementioned studies suggest that if more lenders had been examined under the CRA, some of the negative effects of the crisis could have been averted. Harvard's Joint Center for Housing Studies recommended that CRA's reach should, in the future, cover all mortgage lenders: "The fact that nonbanks, affiliates, and subsidiaries are not uniformly regulated denies consumers equal access to the benefits of legally mandated federal oversight."^{xv}

"I want to give you my verdict on CRA - NOT guilty." - Then Federal Deposit Insurance Corporation (FDIC) Chairman Sheila Bair in a speech at Consumer Federation of America, 2008

"CRA was not a contributor to the mortgage crisis; if it had been, community banks would be at the epicenter and they are not." - Former Office of Thrift Supervision Director John Reich

"Critics of the CRA claim that the wave of risky lending was generated in no small part by banks having been pushed into making these loans to meet their CRA requirements. While not supported by any in depth empirical analysis, this argument has gained enough prominence that a variety of newspapers have written editorials to counter these arguments. There is a variety of empirical evidence that supports the view that CRA's requirements played little or no role in producing the foreclosure crisis." - Department of Housing and Urban Development (HUD) report 'Root Causes of the Financial Crisis', which can be found online at http://www.huduser.org/publications/pdf/Foreclosure_09.pdf.

"So, just to be clear, the idea that [CRA] caused the subprime crisis, the numbers just don't match up." - HUD Secretary Shaun Donovan, at a 2008 event in Brooklyn with New York Mayor Michael Bloomberg

"It is wrong to blame government policies for increasing homeownership for this Wild West market." - Harvard University Prof. and former HUD official, Office of Thrift Supervision (OTS) Director Nicolas Retsinas in a Oct. 8, 2008 Boston Globe opinion piece

"Predatory lending and greed are the root causes of the current downturn. To place the blame on those most victimized by those very practices is scapegoating of the worst kind and offends every sense of truth and moral responsibility." - Rep. Joe Baca in a Joint Coalition Statement from the Tri-Caucus Coalition



ⁱ Dugan, John (2008). November 19, 2008 Remarks Before the Enterprise Annual Network Conference. Accessed online at: <http://www.occ.treas.gov/news-issuances/speeches/2008/pub-speech-2008-136.pdf>.

ⁱⁱ Park, Kevin (2010). "CRA Did Not Cause the Foreclosure Crisis." Center for Community Capital, University of North Carolina, Chapel Hill. Accessed online at: ccc.unc.edu/cra.

ⁱⁱⁱ Kroszner, Randall S. "The Community Reinvestment Act and the Recent Mortgage Crisis." Speech given at the Confronting Concentrated Poverty Policy Forum, Board of Governors of the Federal Reserve System, Washington, DC, December 3, 2008. Accessed online at: <http://www.federalreserve.gov/newsevents/speech/kroszner20081203a.htm>.

For further information:

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Avery, Robert B., Raphael W. Bostic, Paul S. Calem, and Glenn B. Canner (2007). "The 2006 HMDA Data." Federal Reserve Bulletin 94: A73-A109. Accessed online at: <http://www.federalreserve.gov/pubs/bulletin/2007/pdf/hmda06draft.pdf>.

^{iv} Board of Governors of the Federal Reserve System (1993). "Report to the Congress on Community Development Lending by Depository Institutions," pp. 1-69.

Board of Governors of the Federal Reserve System (2000). "The Performance and Profitability of CRA-Related Lending," pp. 1-99.

^v Laderman, Elizabeth and Carolina Reid (2009). "CRA Lending During the Subprime Meltdown." Federal Reserve Bank of San Francisco. Monograph. 2009 - p. 115-133. Accessed online at: http://www.frbsf.org/publications/community/cra/cra_lending_during_subprime_meltdown.pdf. See page 124.

^{vi} Park, Kevin (2010). "CRA Did Not Cause the Foreclosure Crisis." Center for Community Capital, University of North Carolina, Chapel Hill. Accessed online at: ccc.unc.edu/cra.

^{vii} Joint Center for Housing Studies at Harvard University (2002). "The 25th Anniversary of the Community Reinvestment Act: Access to Capital in an Evolving Financial Services System." Accessed online at: <http://www.jchs.harvard.edu/publications/governmentprograms/cra02-1.pdf>. See page 7.

^{viii} Apgar, William C. and Ren S. Essene (2009). "The 30th Anniversary of the CRA: Restructuring the CRA to Address the Mortgage Finance Revolution." A study by the Federal Reserve Bank of Boston and the Joint Center for Housing Studies, Harvard University, published in *Revisiting the CRA: Perspectives on the Future of the Community Reinvestment Act*, a joint publication of the Federal Reserve Bank of Boston and the Federal Reserve Bank of San Francisco. See page 12.

^{ix} Barr, Michael and Gene Sperling. "Poor Homeowners, Good Loans." New York Times Editorial. October 18, 2008. Accessed online at: <http://www.nytimes.com/2008/10/18/opinion/18barr.html>.

^x Ding, Lei, Roberto G. Quercia, Wei Li, and Janneke Ratcliffe (2010). "Risky Borrowers or Risky Mortgages: Disaggregating Effects Using Propensity Score Models." Center for Community Capital, University of North Carolina, Chapel Hill. May 17, 2010 Working Paper. Accessed online at: <http://www.ccc.unc.edu/documents/Risky.Disaggreg.5.17.10.pdf>.



^{xi} Brooks, Rick and Ruth Simon. "Subprime Debacle Traps Even Very Credit Worthy: As Housing Boomed, Industry Pushed Loans to Broader Market." Wall Street Journal. December 3, 2007. Accessed online at: <http://online.wsj.com/article/SB119662974358911035.html>.

^{xii} Chomsisengphet, Souphala and Anthony Pennington-Cross (2006). "The Evolution of the Subprime Mortgage Market." Federal Reserve Bank of St. Louis Review. January/February 2006. Accessed online at: <http://research.stlouisfed.org/publications/review/06/01/ChomPennCross.pdf>. See page 38.

^{xiii} Park, Kevin (2010). "CRA Did Not Cause the Foreclosure Crisis." Center for Community Capital, University of North Carolina, Chapel Hill. Accessed online at: ccc.unc.edu/cra.

^{xiv} Apgar, William C. and Ren S. Essene (2009). "The 30th Anniversary of the CRA: Restructuring the CRA to Address the Mortgage Finance Revolution." A study by the Federal Reserve Bank of Boston and the Joint Center for Housing Studies, Harvard University, published in *Revisiting the CRA: Perspectives on the Future of the Community Reinvestment Act*, a joint publication of the Federal Reserve Bank of Boston and the Federal Reserve Bank of San Francisco. See page 12.

^{xv} Apgar, William C. and Ren S. Essene (2009). "The 30th Anniversary of the CRA: Restructuring the CRA to Address the Mortgage Finance Revolution." A study by the Federal Reserve Bank of Boston and the Joint Center for Housing Studies, Harvard University, published in *Revisiting the CRA: Perspectives on the Future of the Community Reinvestment Act*, a joint publication of the Federal Reserve Bank of Boston and the Federal Reserve Bank of San Francisco. See page 27.

