DENNIS J. KUCINICH
10TH DISTRICT, OHIO

2445 RAYBURN HOUSE OFFICE BUILDING
WASHINGTON, D.C. 20515
(202) 225-5871

14400 DETROIT AVENUE
LAKEWOOD, OHIO 44107
(216) 228-8850

PARMATOWN MALL
7904 DAY DRIVE
PARMA, OH 44129
(440) 845-2707

Congress of the United States
House of Representatives
www.kucinich.house.gov

CHAIRMAN,
SUBCOMMITTEE ON DOMESTIC POLICY

COMMITTEE ON OVERSIGHT AND
GOVERNMENT REFORM

COMMITTEE ON EDUCATION AND LABOR

Opening Statement
Congressman Dennis J. Kucinich, Chairman
Domestic Policy Subcommittee
Oversight and Government Reform Committee

"Upholding the spirit of the CRA: Do CRA Ratings Accurately Reflect Bank Practices?"
2154 Rayburn HOB – 2 P. M.
Wednesday, October 24, 2007

Good afternoon and welcome. The Subcommittee on Domestic Policy of the Committee on Oversight and Government Reform will come to order.

This is the third hearing in a series of hearings on subprime lending and the response of regulators. Our first hearing in March examined the subprime mortgage industry and the problem of foreclosure, the pay day lending industry and the enforcement of the CRA. In our second hearing, the Subcommittee took a closer look at the foreclosure crisis in Cleveland and its relationship to the Federal Reserve Board. And in this hearing, "Upholding the spirit of the CRA: Do CRA ratings accurately reflect bank practices?" we are exploring the coincidence of persistent discrimination in lending and a 98% passing rate among banks on their CRA exams. We hope that by the end of this hearing we can identify a few solutions that will enhance the CRA and its enforcement by the regulators so that it better reflects discriminatory practices by regulated banks.

Congress enacted the CRA in 1977 to combat redlining practices by banks. As mayor of Cleveland at the time, I was one of the first mayors to sign a CRA agreement to hold banks to account for their history of discrimination. CRA made illegal the banking practice of arbitrarily and systematically refusing service to low- and moderate-income and minority communities. The CRA applies to federally insured depository institutions and is enforced by regulatory review. Enforcement is delegated to four federal agencies, the Federal Deposit Insurance Corporation, the Federal Reserve System, the Office of Thrift Supervision, and the Comptroller of the Currency.

The regulatory banking agencies have a powerful enforcement tool: the authority to deny or approve a banking institution's application for a new charter, a new branch, a merger, or an acquisition. Banking regulators exercise this authority based on an institution's CRA rating, which measures the banks' performance to meet the credit needs of its communities. Failure to meet the credit needs of its communities can translate, via the

CRA rating, into a missed opportunity for the bank to acquire more wealth, making the CRA rating a critical incentive for banks to serve its minority and low and moderate income communities.

But since 1990, the banking regulators gave failing grades in just 225 of 60,194 CRA exams. Take a look at this slide **(point to slide 1)**. Today 98.4% of all regulated banks pass the CRA. Compare this to 1990 when only 90.4% of regulated banks received a passing CRA rating. Does the significant rise of the number of banks that pass the CRA suggest that in 2007, banks are improving their lending practices? Does a passing grade accurately reflect bank practices?

Not necessarily.

Take a look at this slide **(point to slide 2)**. According to a recent study conducted by the National Coalition for Community Reinvestment, 24 out of the 25 largest U.S. metropolitan municipalities and their surrounding areas have fewer banking branches in densely populated urban centers than the less populated suburbs.

Today, nearly 14 million households, or 21 percent of all US households, are 'unbanked,' meaning that they have no relationship to a bank or a credit union. Other households are 'underbanked' in that they have deposit accounts but often seek services from payday lenders and check cashers.

Not only do minority communities have less access to banks, but according to the 2004 HMDA data, when they do have access, African-American and Latino populations receive a disproportionate share of higher rate home loans. **(Point at slide 3)** Even after accounting for differences in risk, borrowers of color were more than 30 percent more likely to receive a higher rate loan than white borrowers.

So our question is this: how can banks be passing the CRA at such high rates while the HMDA data show statistically significant racial discriminatory lending practices and while bank services for low- and moderate-income communities are diminishing? We invited the federal banking regulators here today to help us answer that question.

In exploring this conundrum ourselves, the Subcommittee identified several regulatory and statutory issues that raised red flags. These include:

- the discretionary latitude exercised by banking regulators;
- the lack of transparency of the CRA exam process; and
- the incongruency of the 1999 Gramm-Leach-Bliley Act and the CRA.

The regulations surrounding the review of banks are broad and undefined. Although the regulations stipulate that evidence of discrimination adversely impact a bank's CRA rating, the regulations do not stipulate a mandatory downgrade in the face of such evidence. As we dug deeper into the matter, we found cases where the Department of Justice (DOJ) prosecuted a bank for Fair Housing and Equal Credit Opportunity Act violations, while simultaneously the federal regulator issued the bank a passing CRA rating.

Case in point: In 2006, the DOJ filed suit against Old Kent Bank for violating the FHA and the ECOA. In its complaint, the DOJ alleged that in spite of the regulation, Old Kent Bank circumscribed its lending area in the Detroit Metropolitan Statistical Area to exclude most of the majority African American neighborhoods by excluding the City of Detroit. **(Point to slide 4)**

Between 1997 and 2001, the Federal Reserve Bank not only gave Old Kent passing CRA ratings, but it also approved Old Kent's significant branching activity. In January 1996, Old Kent had 18 branches in the Detroit MSA. Not a single one was in the City of Detroit. By March 2000, it had expanded to 53 branches, located in every county of the Detroit MSA except for the City of Detroit which at that point was 81% African-American.

How can the Fed see this map, refer the case to the DOJ for prosecution and give Old Kent Bank a passing CRA rating? We asked the Fed that question and were told that in the Fed's discretion, the bank's practices were reasonable and legal.

If discretionary latitude is broad enough to deem this donut-hole **(point to slide 4)** reasonable, then perhaps it is too broad.

But regulatory discretion does not explain everything. Something in the regulations makes it possible for a CRA rating to not reflect discriminatory practices.

In 1999, the Sixth Circuit Court of Appeals upheld a finding against Flagstar Bank for discrimination against minority borrowers. In 2001, a federal court in Indianapolis found a written pricing policy developed by Flagstar so overtly discriminatory that it ruled against Flagstar on summary judgment. During the period of Flagstar's violations, the federal regulator, the Office of Thrift Supervision conducted five CRA examinations. It awarded Flagstar four "satisfactory" ratings and one "outstanding" rating. Significantly, the outstanding rating was awarded after the summary judgment finding in 2003.

How can Flagstar be awarded with passing CRA grades while it is being prosecuted for its discriminatory practices?

We learned that one way a bank can mitigate a low CRA rating is by agreeing to take corrective action to address its discriminatory practices. Discriminatory practices are found during a fair lending exam, the findings of which are not made public, unlike the CRA exam. Not only is the fair lending exam secret but so too are the negotiations on corrective actions between the regulatory agency and the bank.

This, I think, flies in the face of the CRA's spirit, which was born out of public protest and sustained by public participation. According to Treasury Department, CRA-related home lending in low- to moderate-income communities increased in metropolitan areas in which lending institutions and community groups negotiated CRA agreements. An informed public and a participating public is the hallmark of the CRA. By negotiating corrective actions behind closed doors, banks and their regulators create generic solutions that may not be appropriate for all. In exchange for generic solutions and the exclusion of public participation, banks like Flagstar maintain their good reputations and are afforded the privileges associated with passing CRA scores.

Then there's another problem that has nothing to do with the regulations at all but instead is a problem with the law.

In March 2000, the Gramm-Leach-Bliley Act effectively allowed financial institutions to merge with insurance companies, securities underwriting firms, and mortgage lending companies for the first time in history. But the CRA was not amended to reflect this financial development. As a result, while a loan offered by a bank or thrift is subject to CRA review, that same loan evades CRA scrutiny if it is offered by that bank or thrift's affiliated mortgage company, finance company, or other non-depository affiliate. This loophole enables banks to move their financial assets to non-covered affiliates to reduce their CRA obligations. Subprime borrowers are especially vulnerable to these unregulated lenders. According to RealtyTrac Inc., which compiles statistics on home ownership, last month foreclosures totaled 225,538—double the number a year ago. Would the numbers be different if these companies were subject to CRA obligations? Has this legal loophole enabled a surging foreclosure crisis? And if this is indeed the case, has Congress allowed the CRA to become obsolete in certain respects?

We hope that with the insight of the federal banking regulators as well as community groups and advocates, we can answer some of these questions and find a way to restore the CRA and uphold its spirit.