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Clinton Added Teeth To CRA, Obama Turned Them Into Fangs

By Paul Sperry – January 24, 2013

Despite new evidence the Community Reinvestment Act led to riskier lending and played a key role in the subprime mortgage crisis, the Obama administration is broadening the anti-redlining regulation's authority and scope, spooking bankers.

A recent study by the National Bureau of Economic Research, the nation's pre-eminent economic research group, states that the CRA "clearly" had a major impact on the flood of subprime loans made in the late 1990s and 2000s, which directly led to the housing crisis.

By quietly expanding the regulation, analysts say President Obama is picking up where President Clinton left off in April 1995, when he rewrote rules for what had been a largely toothless law as first drafted in 1977.

Through executive orders, Clinton set strict numerical lending targets for banks in "underserved" neighborhoods, while ordering regulators to crack down on alleged bank redlining.
The new rules for the first time mandated that banks use "innovative" or "flexible underwriting practices." Compliance required banks to pass a heavily weighted "lending test" or suffer holds on expansion plans.

The CRA overhaul "has been a disaster," said ex-BB&T CEO John Allison in his recent book on the financial crisis. He argued it's forced "banks to participate in making high-risk housing loans to low-income buyers who would not meet traditional bank lending standards."
Added Allison, who now heads the Cato Institute: "The default rates on these low-income loans are extraordinarily high."

Still, the Obama administration wants banks to step up approval of such low-income mortgages. And it's using the CRA to spur more lending, including:

• Forcing banks through threat of prosecution to expand their CRA assessment areas to include inner-city areas blighted by subprime foreclosures, where they are compelled to invest in new brick and mortar.

Many banks, in fact, are under direct federal orders to open new branches or ATMs in high-risk and unprofitable areas of Detroit, St. Louis and other cities hit hardest by the recession.
"If your assessment area looks like something you can eat — a bagel or is crescent shaped — that should be a red flag for your bank," senior Department of Justice official Tom Perez warned bankers serving areas mainly outside the inner city.

"DOJ wants banks to have a physical presence in the inner city," Washington-based Buckley Sandler LLP recently told clients, adding that "banks should carefully monitor loan data to determine whether an appropriate volume of loan originations emanate from minority areas."

• Ordering bank defendants accused of lending bias to underwrite riskier CRA loans at discounted rates.
For instance, Justice has ordered First United Security Bank of Alabama to "ensure that residential and CRA small business loan products are made available and marketed in majority African-American census tracts," while offered on terms "more advantageous to the applicant" than normal.

• Toughening CRA enforcement by bank examiners, who are giving more banks negative ratings on their CRA exams and crippling their ability to acquire or merge with other institutions. Federal data show the share of banks receiving failing grades has more than doubled to 4% from 1.5% in 2007.

• Factoring the findings of the Consumer Financial Protection Bureau, the Dodd-Frank Act-created agency empowered with investigating fair-lending violations, into CRA ratings.

• Broadening CRA examination guidelines to include loan "pricing discrimination," and instructing examiners to take a closer look at improper "steering" of minority borrowers into subprime loans with higher interest rates and fees.

• Using the threat of CRA "noncompliance" and denial of expansion plans to pressure bank defendants into settling "fair lending" cases, while scaring other banks into lending in low-income minority areas where the banks aren't located.

"Regulators have now said that banks will not be permitted to proceed with any expansion if they are the target of these pending DOJ actions," complained Independent Community Bankers of America President Camden Fine in a 2011 letter to Attorney General Eric Holder.

• Pressuring banks to fund HUD's new $7 billion Neighborhood Stabilization Program to earn CRA credits under a new "community development" test.