

# A More Modern CRA for Consumers

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When the Community Reinvestment Act (CRA) was enacted in 1977, low-income American communities, especially in cities, were suffering from disinvestment and a lack of credit availability. The CRA requires banks and thrifts operating in and near those communities to lend in them, consistent with safe and sound operations. Since 1977, the financial services system and financial needs of low- and moderate-income consumers have changed dramatically. At least until recently, when credit has tightened, we have become concerned not only about access to credit, but also about the quality of credit. Moreover, consumers have greater need for quality, affordable transactional, saving, investment and insurance products. The combination of the CRA's flexible affirmative mandate and the public availability of CRA examinations has been extremely powerful. This article asserts that while the CRA itself needs updating, its basic elements can and should be extended to a broader array of consumer financial products and providers.

## Thirty Years of the CRA

In 1977, concerned about the denial of credit to lower-income communities, both minority and white, Congress enacted the Community Reinvestment Act. Under the CRA, "regulated financial institutions have

[a] continuing and affirmative obligation to help meet the credit needs of the local communities in which they are chartered." The statute also requires that federal bank regulators both "assess the institution's record of meeting the credit needs of its entire community, including low- and moderate-income (LMI) neighborhoods, consistent with safe and sound operation of such an institution" and that they "take such record into account in its evaluation of an application for a deposit facility by such institution."<sup>1</sup> Bank regulators award institutions one of four ratings, from Outstanding to Substantial Noncompliance, and they make the examination reports (called Public Evaluations) public.

In the 30 years since its enactment, the CRA has substantially changed how banks and thrifts view and serve low- and moderate-income communities and consumers. These communities have seen billions, perhaps trillions, of dollars of credit and investment flow to them as a result of the act, other collateral laws such as the Home Mortgage Disclosure Act (HMDA),<sup>2</sup> various antidiscrimination statutes, and Fannie Mae and Freddie Mac obligations.<sup>3</sup> Although those subject to the CRA once complained bitterly about it, that time has largely passed.

In the same 30 years, the U.S. financial system has also seen major changes. Even prior to the 2008 financial crisis, the number of banks and thrifts had declined

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1 12 USC 2901.

2 12 USC 2801. HMDA was enacted in 1975 and requires virtually all institutions making residential mortgage loans to maintain records on applications, denials, income, race, gender, location, use, and since 2004 for certain loans, the price of individual loan transactions, and to report this information to the federal banking regulatory agencies or the Department of Housing and Urban Development. The Federal Financial Institutions Examination Council makes the information for individual institutions and geographies available to the public in paper and electronic form, and individual institutions are required to have their information available to the public at their offices.

3 According to the Joint Center for Housing Studies, "CRA has expanded access to mortgage credit; CRA-regulated lenders originate more home purchase loans to lower-income people and communities than they would if CRA did not exist." See "The 25th Anniversary of the Community Reinvestment Act: Access to Capital in an Evolving Financial Services System" (Cambridge, MA: Harvard University, March 2002), available at [www.jchs.harvard.edu/research/crareport.html](http://www.jchs.harvard.edu/research/crareport.html)). Eugene A. Ludwig, Comptroller of the Currency, said in remarks at the U.S. Treasury on July 15, 1997: "Since CRA became law in 1977, we have witnessed more than \$215 billion of loan commitments for low and moderate income lending. . . . Since 1993 . . . home mortgage loans to low and moderate income census tracts have risen by 22 percent, more than twice as fast as the rate of growth in all home mortgage loans. In the past four years, banks have invested four times as much in community development projects as they did in the whole previous thirty years." See full remarks at [www.occ.treas.gov/ftp/release/97-65.txt](http://www.occ.treas.gov/ftp/release/97-65.txt)). Likewise, Senator Levin, quoting Chairman Alan Greenspan, 145 Cong. Rec. S4775-76 (1999), said "CRA has 'very significantly increased the amount of credit in communities' and the changes have been 'quite profound.' In 1997 alone, almost 2,000 banks and thrifts reported \$64 billion in CRA loans, including 525,000 small business loans worth \$34 billion; 213,000 small farm loans worth \$11 billion; and 25,000 community development loans totaling \$19 billion."

precipitously. Those that remain are, in general, far larger and geographically disbursed, a trend that shows signs of accelerating, not slowing down. Moreover, both nonbank financial institutions (such as check cashers) and the capital markets now have far greater impact on the financial and economic lives of low- and moderate-income consumers and communities than they did in 1977.

### ***The Need for Greater Access in a New World of Financial Services***

From a consumer perspective, the current market troubles have demonstrated that although access to credit is critical, so too is the need for credit that is high quality and fairly priced. In an economy that is moving away from cash and toward greater global connectivity, consumers need well designed and fairly priced transactional services, including remittance services. The nearly nonexistent national savings rate coupled with the many families who have no or limited assets, also underscore the need for savings and investment opportunities that are easy to access and use.<sup>4</sup>

From a community perspective, both branch closures and the consolidation of the banking industry have reduced access to bank services and decision makers and to the talents and leadership of local bankers in meeting community economic development needs. At the same time, community-based organizations, including community development corporations, Community Development Financial Institutions, loan funds, counseling agencies, advocates, and others, have expanded to serve these communities directly and to leverage the efforts of banks and thrifts operating under the CRA.

The bulk of discussion about the CRA is focused on community investment and on home mortgage lending. This is not surprising given that measurement of activity in these two areas is relatively straightforward (HMDA makes measuring residential lending particularly easy),

and regulators and outside forces have kept up a steady stream of questions about “how much are you doing, where, and for whom?” Intermittently, critics have taken on the Service Test, which attempts to measure how well banks serve customers other than through loans, arguing that it is misguided or simply ineffective in either measuring or encouraging banks and thrifts to provide quality financial services in lower-income communities.<sup>5</sup>

This article, in contrast, asks whether the framework of the CRA—a relatively broad affirmative mandate to serve—can be the basis for substantially improving the financial services offered to consumers of all income levels, in all communities, but with a special focus on the needs of low- and moderate-income consumers. It considers the question with respect to both the banks and thrifts already covered by the CRA and the many other types of organizations that also provide financial services to consumers.

### **The Changing Face of Consumer Financial Services**

Since the CRA was enacted, consumer financial services, particularly for those of modest incomes, have changed dramatically. Consumers have moved from an economy in which cash and, to a lesser extent, checks were the major way of transacting business, paying bills, and getting paid to one in which only one-fifth of retail transactions are made in cash, and check use is declining in favor of credit and debit cards and ACH transactions.<sup>6</sup>

To purchase a large item in 1977, consumers sought a term loan from their bank, and for smaller transactions, they used independent consumer finance companies and retailers. Today, a bank term loan (other than for a car, boat, or house) is rare, the independent finance companies have largely been acquired by banks, and credit cards are ubiquitous. In 2004, approximately

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4 For information on low savings rates, see Department of Commerce, Bureau of Economic Analysis, “Personal Savings Rate (online chart, 2008), available at <http://www.bea.gov/briefrm/saving.htm>. The savings rate has been below one percent since 2005, although for the second quarter of 2008, it was more than two percent. This was likely due to the federal stimulus checks that families received, largely in May, when the rate shot up to 4.9 percent. Personal savings then declined to 2.5 percent in June. For information on poverty, see Signe-Mary McKernan and Caroline Radcliffe, “Enabling Families to Weather Emergencies and Develop: The Role of Assets.” (Washington, DC: Urban Institute, 2008), available at <http://www.urban.org/publications/411734.html>.

5 See, e.g., Kelly Cochran, Michael Stegman, and Robert Faris, “Creating a Scorecard for the CRA Service Test: Strengthening Banking Services Under the Community Reinvestment Act” (Washington, DC: Brookings Institution, 2003), available at [http://www.brookings.edu/papers/2003/01childrenfamilies\\_stegman.aspx](http://www.brookings.edu/papers/2003/01childrenfamilies_stegman.aspx).

6 On retail transactions see Ronald Mann, *Charging Ahead: The Growth and Regulation of Payment Card Markets* (New York: Cambridge University Press, 2006) p. 10, data as of 2003). On rise of debit cards, see Federal Reserve, *2007 Federal Reserve Payments Study* (Washington, DC: U.S. Federal Reserve, December 2007), available at <http://www.federalreserve.gov/newsevents/press/other/20071210a.htm>.

75 percent of American households held a credit card, and in 2008, nearly \$1 trillion in credit card debt was outstanding.<sup>7</sup> But the advent of credit scoring combined with the demise of usury laws has made credit more expensive than in the past, in both interest and fees. During this current crisis, all types of credit have become scarce, particularly for those of modest means or with less-than-pristine credit records. These changes mean that pricing and terms are as big a concern as access to credit.

Similar changes have occurred in the mortgage market. Until the current mortgage crisis, mortgage originations and funding had shifted from banks and thrifts to origination through broker and correspondent channels, often for sale to independent mortgage companies, with funding by the capital markets. Although the large independent mortgage banks have ceased to exist, and mortgage credit in general has dried up, it is unlikely that originations will fully move back to retail banking. The sheer scale of the housing market, even if we assume a return to pre-2000 origination levels, suggests brokers will continue to play a role, but that all those who are part of the mortgage origination chain, including brokers, will be required to take some responsibility for the performance of the loan.

Other areas of financial services have also seen major changes. The number of Americans who were born abroad climbed from approximately 14 million in 1980 (6.2 percent of the population) to 33.5 million in 2003 (11.7 percent of the population), creating demand for a new financial service: remittances.<sup>8</sup> The stock market has also seen a surge of new players. Whereas in 1977 few Americans invested in financial instruments beyond a savings account, as of 2004, one in five American families owned stocks and 15 percent owned mutual funds. Nearly one-half had retirement accounts.<sup>9</sup> These products are generally provided by entities other than banks and thrifts, including broker-dealers and insurance companies.

### ***The Growing Ranks of the “Unbanked”***

These broad changes in consumer financial services have uniquely affected lower-income Americans. The combination of a shrinking cash economy, the consolidation of the bank and thrift industries (frequently accompanied by fewer branches in minority and lower-income communities), and the large number of new immigrants have generated additional needs and introduced new players to the system. Consumers need ways to turn paychecks into cash, send money to native countries, and borrow money—ranging from small sums for an emergency to home mortgages based on unconventional income sources or streams. Nonbank financial service providers have become ubiquitous in lower-income communities, including check cashers, whose services frequently include remittances, bill pay, and small dollar credit; other small-dollar lenders such as payday lenders, pawn shops, and auto title lenders; and retailers who offer general purpose, reloadable, prepaid cards in addition to their own gift cards. Author Howard Karger estimates that the United States has more check-cashing and payday lending outlets than McDonald’s, Burger King, Target, Sears, JC Penney, and Wal-Mart stores combined.<sup>10</sup>

The alternative sector is frequently characterized as high-priced and predatory, but it also provides products and services that meet the financial services needs of a significant swath of the population that banks, thrifts, and credit unions are not serving fully.<sup>11</sup> Although the Federal Reserve’s Survey of Consumer Finance estimates that as of 2004, about ten percent of families lacked a checking account, other surveys suggest that the number of individuals without a checking or savings account reaches nearly 30 percent among lower-income populations.<sup>12</sup> As Michael Barr noted in his recent study of lower-income consumers in Detroit:

7 For data on credit cards, see Brian K. Bucks, Arthur B. Kennickell and Kevin B. Moore, “Recent Changes in U.S. Family Finances: Evidence from the 2001 and 2004 Survey of Consumer Finances,” *Federal Reserve Bulletin* (March 2006), p. A31. For data on outstanding debt, see “Federal Reserve Statistical Release G.19” (Washington, DC: Federal Reserve, July 8, 2008).

8 U.S. Census Bureau, “Table 1. Nativity of the Population and Place of Birth of the Native Population: 1850 to 1990” (Washington, DC: Census, March 9, 1999), available at [www.census.gov/population/www/documentation/twps0029/tab01.html](http://www.census.gov/population/www/documentation/twps0029/tab01.html); U.S. Census Bureau, *The Foreign-born Population in the United States: 2003* (Washington, DC: Census, August 2004).

9 Bucks, “Recent Changes in U.S. Family Finances” p. A13.

10 Howard Karger, *Shortchanged: Life and Debt in the Fringe Economy* (San Francisco: Berrett Kohler Publishers, 2005), p. 6.

11 Karger, *Shortchanged*.

12 Bucks, “Recent Changes in U.S. Family Finances,” p. A15. For the other surveys, see, e.g., Ellen Seidman et al., “A Financial Services Survey of Low- and Moderate-Income Households,” (Chicago, IL: Center for Financial Services Innovation, 2004), available at [www.cfsinnovation.com/research-paper-detail.php?article\\_id=293](http://www.cfsinnovation.com/research-paper-detail.php?article_id=293); Barr, “Financial Services, Saving and Borrowing.”

Though associated with high fees both banked and unbanked sample members often describe AFS [alternative financial services] transactions as convenient. At the same time, bank accounts are usually not well structured to serve LMI households. Bank fees are quite high, and over half of banked LMI households reported paying minimum balance or overdraft or insufficient fund fees in the previous year. The financial services mismatch between the needs of LMI households and the products and services offered to them largely constrains LMI households to choose among high fee, ill-structured products offered by banking and AFS institutions.<sup>13</sup>

The Center for Financial Services Innovation recently completed a national study of un- and underbanked consumers, a group that includes approximately 40 million households, or about 36 percent of American households.<sup>14</sup> This group has a median household income of \$26,390. Nearly one-half (47 percent) work full-time, and 63 percent own their homes. The group is 60 percent white, 19 percent Hispanic, and 16 percent non-Hispanic black. The survey found that nearly one-half of the group did not have a checking or savings account, that is, they were “unbanked,” although about one-half of that number had had an account at some point in the past. The most frequent reason for not having a bank account was not having enough money to make one useful. The Detroit study reached similar conclusions, but also noted that three-fourths of the unbanked said they would like to open a bank account in the next year, and one-third had recently looked into getting a bank account.<sup>15</sup>

## A New Paradigm for Responsibility in Consumer Financial Services

Both the changing consumer financial services landscape in general and the particular problems that lower-income consumers face as they attempt to transact business (borrow, save, invest, and insure their possessions) strongly suggest that it is time for a new paradigm for consumer financial services. To address the substantial and continuing changes in the industry, the country needs a proposal just as bold and just as flexible as the CRA was 30 years ago. I suggest the following:

Any financial institution that provides an essential consumer product must make that product available in a fair and transparent manner to low- and moderate-income consumers in all communities in all broad geographies in which the entity does more than an incidental amount of business in the product.<sup>16</sup>

### **Fairness and Transparency**

Fairness and transparency are central principles in the financial services sector. But these principles often apply differently to low- and moderate-income consumers. The reasons for these different applications include a smaller margin for error and lack of capital on which to base a recovery when something goes wrong; generally lower education levels among participants; less access to quality and timely financial advice; and, particularly in the last 15 years, a younger population often with limited experience with the American financial system.

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13 Barr, “Financial Services, Saving and Borrowing” p. 3.

14 Center for Financial Services Innovation, “The CFSI Underbanked Consumer Study, Underbanked Consumer Overview and Market Segments.” Fact Sheet. (Chicago, IL: CFSI, June 8, 2008), available at [www.cfsinnovation.com/research-paper-detail.php?article\\_id=330366](http://www.cfsinnovation.com/research-paper-detail.php?article_id=330366). The 40 million includes both unbanked (no checking or savings account) and underbanked (having an account, but having made one or more nonbank financial transactions in the prior 30 days).

15 See Barr, “Financial Services, Saving and Borrowing” pp. 13-14.

16 The paradigm would not explicitly cover financial institutions that do not provide products to consumers directly or through agents, such as investment banks and Fannie Mae and Freddie Mac. However, the responsibilities institutions have in directly serving consumers should carry through to their investment activities. See Letter from Edward B. Kramer, Deputy Superintendent of Banks, State of New York Banking Department, “Due Diligence Recommendations Concerning the Eligibility of Loan Purchases and Investments for Consideration Under the Community Reinvestment Act,” July 26, 2001, available at <http://www.banking.state.ny.us/lt010726.htm>. In addition, these institutions might well be covered by some version of the CRA Investment Test.

In this context, fair then means that an entity providing essential consumer financial services to the general public, directly or through agents, must abide by the following principles:

- Essential financial services must meet the needs and desires of low- and moderate-income consumers, with sufficient market research to accurately assess those needs;
- Essential financial services must be offered at equitable prices and terms, on the basis of cost and an accurate assessment of risk;
- Analysis of potential profitability over time, need for capital, and other investment criteria must be done on a basis that is no less favorable for service to low- and moderate-income consumers than it is for wealthier consumers.

For example, if a bank offers overdraft protection based on a line of credit or a tie to a savings account to customers who open checking accounts in branches in suburban neighborhoods, it would also be required to investigate whether consumers in lower income communities would prefer this type of protection to a fee-based overdraft program. It would then analyze the potential profitability of such programs in both types of communities on an equal basis (e.g., if profitability is analyzed on a product rather than customer basis in one place, the same type of analysis should be used in the other), and offer (or decline to offer) the product in both places at prices that accurately reflect cost and risk on a similarly individualized basis.

Transparency has two essential dimensions, one for consumers and one for the public:

- Firms must provide actual and potential customers with quality service and accurate information about the terms of products, delivered in a timely and understandable fashion, including realistic information about risks;
- Firms must provide the public (or if information is proprietary, a government intermediary) with information on how the firm provides essential consumer financial services; and that information must be available in a manner and with sufficient

quality, quantity, and timeliness to allow persons outside the firm to accurately assess the extent to which a firm meets its obligations, both during the current period and over time.

Taken together, these two concepts would require better and more accurate disclosure to consumers about product terms and risks—the one-page mortgage disclosure document suggested by Alex Pollock of the American Enterprise Institute is an example<sup>17</sup>—and the extension of HMDA reporting to other products such as credit cards and small consumer loans.

This paradigm thus focuses on the effective development, marketing, and distribution of well-designed and understandable consumer products and services, and it imposes a requirement of equity across communities and consumers of all types. It concentrates the attention of business, the public, and government on what is important to consumers, and uses the market forces generated by consumers with the knowledge and resources to demand high-quality financial services to extend the reach of those products and services to the rest of the market.

## Products and Services Subject to the New Responsibility Paradigm

The extent of coverage of products under this new paradigm is an important consideration. It is critical not to pull back on current coverage of the CRA. At the same time, it is also clear that not all products, services, or financial institutions should be covered by CRA-style regulation. To take an extreme example, it is neither necessary nor an appropriate use of scarce enforcement resources to ensure that hedge fund investment opportunities be available to low- and moderate-income consumers. However, coverage should not be excessively limited, or too tied to current economic conditions and financial structures and opportunities.

A useful way to think about products and services that should be covered by the CRA is to focus on those financial products and services that are essential to full and active participation in the American middle class. These include products and services to meet transactional, credit, saving and investment, and insurance needs. Products and services should be considered “essential”

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17 See Alex Pollock, “The Basic Facts About Your Mortgage Loan,” (Washington, DC: American Enterprise Institute, 2007), available at [http://www.aei.org/docLib/20070913\\_20070515\\_PollockPrototype.pdf](http://www.aei.org/docLib/20070913_20070515_PollockPrototype.pdf).

only if the public broadly uses them. Although the items included will likely change over time, by defining them in terms of functionality rather than specific products, we reduce the need for additions or subtractions.

### **Transactions**

With respect to transactions, the ongoing, revolutionary changes occurring with prepaid cards and the likelihood of major breakthroughs in using mobile phones for financial services call for a functional approach.<sup>18</sup> Essential functionalities are converting sources of revenue (particularly paychecks and benefits of all sorts) into useable means of payment; and a means of making timely and secure payments and transfers to savings or investment.

### **Credit**

For credit, “essential” may be defined in terms of likely future credit needs. This, of course, was the area of initial concern under the CRA, and it continues to be critical in providing the leverage for major wealth-building investments such as a home or higher education and to smooth income fluctuations. Thus, essential credit products include short-term credit, whether secured or unsecured, for small amounts; auto credit; mortgage credit, and credit for postsecondary education.

### **Savings and Investments**

Saving and investment were not part of the initial CRA focus, in part because the CRA at the time sought to address the problem that financial institutions in lower-income communities did not reinvest low-income individuals’ savings in their communities. Today, the problem is not so much reinvestment of savings as spurring savings in the first place. It is clear, given the current debt-led economic troubles and low national personal savings rate, that Americans need to save more money.

In 1977, individual access to investment opportunities was limited, but there was less need for such opportunities because defined-benefit retirement plans, in which the employer took responsibility for investment decisions and outcomes, were much more common. This has since changed. The new paradigm should therefore cover: (a) non purpose-limited, short-term savings opportunities; (b) longer-term, low-risk saving and investment

opportunities (e.g., insured accounts, CDs, and Treasury obligations including savings bonds); and (c) investment opportunities such as retirement accounts and tax-advantaged Section 529 education savings plans.

### **Insurance**

Insurance is also an essential product. In most states, drivers must be insured, and mortgage creditors demand homeowner’s insurance. Both types of insurance are important to protecting these assets. It is therefore critical to include automobile and homeowner’s insurance in the new responsibility and accountability regime. Medical insurance, including long-term care coverage, is also highly desirable; a significant share of bankruptcies is caused by uninsured medical expenses. However, this is an issue that goes far beyond the financial services sector and requires a much broader solution.

## **How These Principles Relate to Current CRA Enforcement and Interpretation**

To bring the CRA more fully in line with both the modern financial services system and the principles and scope proposed, some changes are needed. The most important are the following:

- The CRA should cover service to low- and moderate-income consumers in providing an essential product everywhere a bank or thrift does a significant amount of business in any of the essential products. If a firm operates nationally, it should be evaluated on how well it serves low- and moderate-income consumers nationwide with the type of product it is offering nationally. Thus, CRA coverage with respect to mortgage loans should depend on where the firm makes such loans, not where it has deposit-taking branches, as is currently the case.
- Effective public disclosure should be added that covers additional essential products, including the essential transaction and savings products used by low- and moderate-income consumers. Thus, HMDA should be extended to other essential consumer products.

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<sup>18</sup> For example, the advent and spread of reloadable prepaid cards, which can in some instances function as a bank account, would have been unforeseen five years ago; the spread of mobile banking has the same potential for dramatic change in the consumer financial services market. For a comprehensive discussion of these and other technologies in the context of lower-income consumers in developing countries, see Consultative Group to Assist the Poor (CGAP), “Regulating Transformational Branchless Banking: Mobile Phones and Other Technology to Increase Access to Finance” (Washington, DC: CGAP, 2008), available at [www.cgap.org/p/site/c/template.rc/1.9.2583](http://www.cgap.org/p/site/c/template.rc/1.9.2583).

- Any for-profit subsidiary or holding company affiliate that provides any of the essential products should be evaluated in the same manner and at the same time as the largest bank or thrift in the holding company group. This would overcome the current situation in which lower quality products offered by a bank or thrift holding company through a subsidiary escape evaluation because they are offered outside of the bank or thrift.
- Consumer protection and fair lending responsibilities must be more firmly embedded in CRA evaluations. This would extend the 2005 regulatory revisions that mandate, when evaluating lending activities, that evaluators assess compliance with the fair lending and consumer protection laws and regulations to cover transactional, saving, and investment offerings.<sup>19</sup> The quality of products, especially credit products, must be considered in addition to the penetration of such products into all communities.
- Incentives should be established that are external to the CRA, potentially including reduced insurance premiums for outstanding performance; as the current troubles in the market remind us, treating consumers well is good for business over the long term. To stimulate better performance and limit grade inflation, the number of Outstanding ratings should be limited, perhaps to a slowly increasing percentage above current levels.

## Extending the Paradigm to Other Essential Functions

Some commentators assert that the CRA, with its requirement that banks and thrifts fully serve all communities in their assessment areas, is to blame for the current financial crisis.<sup>20</sup> There are many reasons to doubt such claims, including timing (CRA was passed and the regulations strengthened long before serious problems arose), the generally higher quality of mortgages made by depository institutions in their assessment areas, and the fact that the worst excesses have occurred as CRA enforcement diminished in the past eight years.<sup>21</sup> However, the most convincing reason not to lay the blame on the CRA is the high proportion of high-priced loans that were made by entities not subject to the CRA.<sup>22</sup> The problem, of course, was that these other institutions were also exempt from the level of consumer protection to which banks and thrifts were subject, and they discovered that lending with fewer limitations to individuals in lower-income communities was highly profitable.<sup>23</sup>

This problem of unequal regulation and enforcement raises a need for some caution with respect to extending the CRA beyond banks and thrifts, particularly for credit products. Although the Federal Reserve and Congress have reduced the regulatory disparity in mortgage lending, enforcement disparities will continue and other types of credit are still under highly variable regulatory schemes.<sup>24</sup> For example, payday lending is

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19 See 12 CFR 345.28(c) (FDIC); 12 CFR 228.28(c) (Federal Reserve); 12 CFR 25.28(c) (OCC); 12 CFR 563e.28(c) (OTS).

20 See, e.g., comments of Larry Kudlow at <http://www.cnbc.com/id/15840232?video=702180420&play=1>. More recent accusations are collected (and rebutted) at Media Matters, September 30, 2008, available at <http://mediamatters.org/items/200809300012>.

21 See Randall Kroszner, "The Community Reinvestment Act and the Recent Mortgage Crisis" (Washington, DC: Federal Reserve Board, December 3, 2008), available at <http://www.federalreserve.gov/newsevents/speech/kroszner20081203a.htm>. For evidence of high-quality mortgages, see See Traiger and Hinckley LLP, "The Community Reinvestment Act: A Welcome Anomaly in the Foreclosure Crisis" (New York, NY: Traiger and Hinckley, LLP, January 7, 2008) available at [www.traigerlaw.com/publications/traiger\\_hinckley\\_llp\\_cra\\_foreclosure\\_study\\_1-7-08.pdf](http://www.traigerlaw.com/publications/traiger_hinckley_llp_cra_foreclosure_study_1-7-08.pdf); and Traiger and Hinckley LLP, "Addendum to: The Community Reinvestment Act: A Welcome Anomaly in the Foreclosure Crisis," (January 14, 2008) available at [http://www.traigerlaw.com/publications/addendum\\_to\\_traiger\\_hinckley\\_llp\\_cra\\_foreclosure\\_study\\_1-14-08.pdf](http://www.traigerlaw.com/publications/addendum_to_traiger_hinckley_llp_cra_foreclosure_study_1-14-08.pdf). For the diminishing enforcement during the past eight years, see Ellen Seidman, "It's Still not CRA," (Washington, DC: New America Foundation: September 22, 2008), available at [www.newamerica.net/blog/asset-building/2008/its-still-not-cra-7222](http://www.newamerica.net/blog/asset-building/2008/its-still-not-cra-7222); Michelle Singletary, "Blame Game Gets Nasty When it Targets the Poor," *Washington Post*, October 12, 2008, p. F1.

22 Robert Avery, Kenneth Brevoort, and Glenn Canner, "The 2006 HMDA Data," *Federal Reserve Bulletin* (December 2007), p. A89.

23 See Edward Gramlich, "Booms and Busts, The Case of Subprime Mortgages" (Jackson Hole, WY: Federal Reserve Board, August 31, 2007), available at [www.kc.frb.org/publicat/sympos/2007/pdf/2007.09.04.gramlich.pdf](http://www.kc.frb.org/publicat/sympos/2007/pdf/2007.09.04.gramlich.pdf).

24 For efforts by the Federal Reserve, see 73 Fed. Reg. 44522 (July 30, 2008). For congressional efforts, see Public Law 110-289 (July 30, 2008).

entirely prohibited in several states (e.g., New York, North Carolina, and Maryland), subject to relatively tight usury caps in others (Ohio and Arkansas), allowed with other types of regulatory protections in others (Illinois), and allowed without significant limitation in still others (California). As we think about extending the CRA, it will be important to coordinate its service requirement with an acceptable minimum standard of consumer protection.<sup>25</sup>

One way to extend the CRA to other types of financial institutions is to replicate the statute, assigning responsibility for examination and enforcement to regulators (to the extent the firms involved are subject to regulatory supervision), or to surrogates such as the U.S. Department of Housing and Urban Development. For credit unions, which are regulated similarly to banks and thrifts (and also the beneficiaries of federal insurance), such extension would seem appropriate, perhaps modifying the credit unions' statutory service obligation to take into account enhanced responsibilities under a new regime. However, for other types of financial services, operating under different types of (or no) supervisory regimes, alternative solutions are likely required. These solutions should take maximum advantage of existing regulatory systems and responsibilities with the aim of achieving equity in result, rather than complete consistency in regulatory methodology.

### **Enhanced Public Reporting**

A first step should be to ensure that any requirement for public reporting and dissemination of information about credit extends beyond residential lending to include all creditors who extend similar types of credit.<sup>26</sup> As HMDA has demonstrated, the obligation to report can be effectively extended to institutions outside federal regulatory jurisdiction when uniform reporting requirements are in effect, when government-supplied software is available, and when a single entity (in the case of HMDA, the Federal Reserve) is responsible for cleaning data, making it public, and doing the initial analysis. Although the Department of Housing and Urban Development is the initial recipient of mortgage data under HMDA, information about other types of credit could

be provided initially to state regulators or directly to the Federal Reserve.

Similarly, public reporting on noncredit services should be tailored to the type of service and should include all those providing such services as a significant part of their business. For example, to ensure banks, thrifts, or credit unions are meeting service obligations, the primary focus might be the incomes of checking and savings account holders. For insurance companies, the information might relate to the characteristics of holders of defined types of policies. Because this information would be industry-specific, it should be gathered and disseminated by industry-specific regulators where such exist, under standards developed in coordination with bank regulators. As with credit information, other types of financial services providers could provide information directly to the Federal Reserve.

### **Increased Regulatory Reach and Enforcement**

Public dissemination of information serves to inform the public and expand the likelihood that those providers who are offering quality products will have a competitive advantage with consumers. However, to ensure that providers are meeting their obligations to serve fairly consumers who may not be able or inclined to take advantage of such data, public dissemination of data must be accompanied by a regulatory regime that evaluates compliance and imposes consequences, both directly on the company and indirectly by increasing public awareness of how an institution is behaving. This aspect is the most difficult part. We cannot expect other regulatory regimes to adopt wholesale the bank regulatory model, and it is unlikely that would even be desirable.

Instead, the principles of the responsibility paradigm should be added to various regulatory regimes in a manner that is consistent with the scope and intent of the particular regime, and that is consistent with and builds on existing and improved consumer-oriented obligations and protections. For state-regulated entities, the appropriate mechanism is likely national legislation establishing principles, a regulatory floor, and a back-up regulatory regime should states not adopt the regulatory minimum.<sup>27</sup>

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25 For a suggestion for how to accomplish this, see Elizabeth Warren, "Unsafe at Any Rate," *Democracy* (Summer 2007), available at [www.democracy-journal.org/article.php?ID=6528](http://www.democracy-journal.org/article.php?ID=6528). Warren proposes a Financial Product Safety Commission modeled on the Consumer Product Safety Commission.

26 This suggestion is already getting some traction. See "Democrats Eyeing HMDA-Like Rules for Nonmortgages," *American Banker*, July 18, 2008.

27 This is similar to the scheme adopted for regulation of mortgage brokers in the Housing and Economic Recovery Act of 2008. See Title V, Pub. Law 110-289 (July 30, 2008).



Integrating the paradigm's principles consistently into disparate regulatory regimes will require consultation and collaboration at both the state and federal levels. Moreover, for financial services not currently subject to any federal supervision and limited state regulation, it is appropriate to consider a combination of enhanced state regulatory authority (and funding), increased responsibility and funding for the Federal Trade Commission, and/or new statutory responsibilities at the state and federal levels, with private rights of action to enforce them.

### **Considering Broad-Based Product Specifications**

Consumer protections have, in general, focused on limiting product terms, including price, marketing, and advertising. Recently, some have proposed an alternative: requirements that products meeting certain criteria be offered first, or that products be limited to those that meet standard terms, with competition permitted only on, for example, price. With respect to mortgages, for example, several behavioral economists have suggested that all home buyers be first offered a 30-year fixed-rate mortgage, and that lenders provide clear disclosure if borrowers turn down the "default" mortgage; lack of reasonable disclosure would be a defense to bankruptcy or foreclosure if an alternative loan turns bad.<sup>28</sup> Ronald Mann has suggested that credit card contract terms be standardized, limiting competition to a small set of clearly identified and relatively easy-to-comprehend terms, such as the interest rate and level of various fees.<sup>29</sup>

In the realm of transaction accounts and on a more limited basis, Michael Barr has suggested a model "starter" account accessible only by debit card, with no overdrafts permitted and with no minimum balance requirement.<sup>30</sup> And states require preapproval of consumer insurance products, although as the post-Katrina experience in New Orleans has demonstrated, this does not eliminate controversy surrounding underwriting, pricing,

or the effectiveness of coverage.<sup>31</sup>

It is worth exploring whether developing a limited number of preferred or default products for the population in general, or developing a more limited subset targeted by a new CRA obligation, could systematically improve the outcomes for consumers of a broadly applied obligation to serve. Such a product set, if accompanied by a safe harbor protection for providers, might also reduce the uncertainty in a requirement for "fair and equitable" treatment of consumers.

### **Prioritizing and Sequencing**

Even considered in the context of existing regulatory regimes, adopting in full a new responsibility paradigm is a major undertaking. It is, however, possible to stage adoption. One possibility is to begin with the products most likely to create major problems for consumers, and the entities that sell those products. The current situation in the credit markets suggests that credit products should be first on the agenda, followed perhaps by investment products. A second scheme would be to stage implementation based on the lack of availability or accountability for essential products. In this scheme, an initial focus could be on transaction products, where federally regulated depositories are not effectively serving all Americans and alternative providers are subject to little scrutiny and public accountability. A third alternative would be to begin where existing statutory and regulatory schemes are most developed and where implementation of the agenda's principles would require relatively modest changes. This suggests that, beyond banks and thrifts, credit unions should be first, followed by insurance companies and their agents, and then securities brokers.

Each alternative has benefits and drawbacks. For example, moving first on credit products might generate the most benefit for consumers, but it would require development and enforcement of more powerful regulatory and

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28 Michael Barr, Sendhil Mullainathan, and Eldar Shafir, "A One-Size-Fits-All Solution," *New York Times*, December 26, 2007, available at <http://www.nytimes.com/2007/12/26/opinion/26barr.html?scp=1&sq=michael%20barr%20mortgage&st=cse>. See also Michael Barr, Sendhil Mullainathan, and Eldar Shafir, "Behaviorally Informed Financial Services Regulation" (Washington, DC: New America Foundation, October 2008), available at [http://www.newamerica.net/files/naf\\_behavioral\\_v5.pdf](http://www.newamerica.net/files/naf_behavioral_v5.pdf).

29 Ronald Mann, "'Contracting' for Credit," 104 *Mich LR* 899 (2006) at 927-28.

30 Michael Barr, et al, "Behaviorally Informed Financial Services Regulation," *op cit* note 27 at 30-31. This account is similar to the Opportunity NYC account that New York City has arranged at a small number of banks and credit unions to hold the proceeds of its conditional cash transfer program. See [http://home2.nyc.gov/html/ceo/downloads/pdf/report\\_opportunity\\_nyc.pdf](http://home2.nyc.gov/html/ceo/downloads/pdf/report_opportunity_nyc.pdf).

31 See Daniel Schwarcz, "Towards a New Approach for Resolving Consumer Insurance Disputes." Working paper (Ann Arbor, MI: Social Science Research Network 2008), available at [http://papers.ssrn.com/sol3/papers.cfm?abstract\\_id=1183482](http://papers.ssrn.com/sol3/papers.cfm?abstract_id=1183482).

enforcement regimes for entities not currently subject to federal supervision. On the other hand, starting by expanding CRA-like obligations to credit unions but ignoring payday lenders, finance companies and independent mortgage bankers would have the virtue of relative simplicity but would exacerbate the competitive inequality in the current regulatory system. But the alternatives also suggest ways to improve, in measured increments, the essential financial products and services consumers need, and the manner in which those services are delivered.

## Conclusion

Thirty years ago, numerous American cities were dying for lack of credit. By enacting the CRA, the federal government challenged the banking industry to help those communities and their residents achieve a better life. Together with related statutes such as HMDA and antidiscrimination and consumer protection laws, the CRA has had a substantial, positive impact in bringing credit and other financial services to low- and moderate-income consumers and communities.

The 30 years since the CRA's adoption have seen massive changes in the number, complexity, and types of financial products consumers use, how they are marketed and accessed, and who provides them. Simultaneously, the increase in homeownership, workforce restructuring, and the decline in employer-provided retirement and health benefits require consumers to take much greater responsibility for their financial health and stability. Many Americans are not doing well in meeting this new responsibility. The mortgage and credit markets are in turmoil with extraordinarily high and rising levels of foreclosures, the personal savings rate is extremely low, bankruptcies are at record levels, and debt burdens

are overwhelming many families. The new responsibility paradigm presented here challenges the entire financial services industry—as the CRA did 30 years ago—to help American consumers do better. ■

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