

## Putting Race Explicitly into the CRA

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The Community Reinvestment Act (CRA) was designed to correct market failures thirty years ago. The reimagining of CRA must address the remnants of twentieth-century market and government failures with twenty-first century solutions. Financial institutions and regulators must revisit the intent of the CRA, which states that regulators are “to assess an institution's record of meeting the credit needs of its *entire community* [emphasis added], including low- and moderate-income neighborhoods, consistent with the safe and sound operation of such institution.”<sup>1</sup> I proffer that the entire community includes racial and ethnic minorities, and the CRA should be expanded to address directly these underserved parts of the community.

Federal Reserve Chairman Ben Bernanke, in his remarks at the Community Affairs Research Conference, identified racial discrimination as the first of several social and economic factors that led to the enactment of the CRA. Chairman Bernanke stated that “the CRA itself focused on the provision of credit to low- and moderate-income communities rather than on discrimination by race, sex or other personal characteristics. Legislation that addressed discrimination in lending explicitly included the Equal Credit Opportunity Act (ECOA)<sup>2</sup> and the Fair Housing Act.”<sup>3</sup> Bernanke stated that the purpose of the CRA was to “rectify market failures.”<sup>4</sup> While the market failures of the 1970s involved access to credit in low-income areas, the market failures of the twenty-first century fall along race lines. The new CRA should address the governmental and market failures associated with racial discrimination and racial market segmentation.

The ECOA and the Fair Housing Act were designed

to address individual acts of discrimination, and while both include provisions to address disparate impact and systemic discrimination, they have failed to adequately address the market failures that perpetrate and perpetuate racial market segmentation and racial discrimination. This is best achieved by explicitly including race in the CRA, a change that would not require any new or enhanced legislative authority. In fact, §3608(d) of the Fair Housing Act states: “All executive departments and agencies shall administer their programs and activities relating to housing and urban development (including any Federal agency having regulatory or supervisory authority over financial institutions) in a manner affirmatively to further the purposes of this subchapter and shall cooperate with the Secretary to further such purposes.”

Current market failures explain why upper-income African Americans in my hometown of Durham, North Carolina, are four times more likely to have a higher-cost loan than whites with similar incomes.<sup>5</sup> Market failures explain the fact that whites represent 55 percent of the population in poverty but only 30 percent of the people living in neighborhoods of concentrated poverty, while three out of four poor African Americans and Latinos live in these neighborhoods. Market failures explain why one in ten African Americans live in neighborhoods of concentrated poverty compared to one in 100 whites.<sup>6</sup> Market failures explain why rural and urban communities share histories of disinvestment and spatial isolation and yet experience poverty differently. Any revisions to the CRA must address these failures directly and require financial markets to adopt corrective measures.

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1 12 U.S.C. 2901.

2 15 U.S.C. 1691 et seq.

3 42 U.S.C. 3601 et seq.

4 Ben S. Bernanke, “The Community Reinvestment Act: Its Evolution and New Challenges,” *The Community Affairs Research Conference, Federal Reserve Board, Washington, DC, 2007.*

5 National Community Reinvestment Coalition, “Income Is No Shield Against Racial Differences in Lending II: A Comparison of High-Cost Lending in America’s Metropolitan and Rural Areas,” Washington, DC, 2008.

6 Jason Reece, “Will you be my neighbor? Housing and neighborhood diversity in the US,” lecture, February 19, 2008, Kirwan Institute, Ohio State University; and Reece, “Race, Class, and Opportunity: Understanding the Convergence and Divergence of Race and Class in the US.,” lecture, January 16, 2008, Kirwan Institute. Both at <http://www.kirwaninstitute.org/publicationspresentations/presentations/2008.php>.

Throughout American history there have been government failures that have explicitly restricted access and opportunity for racial and ethnic minorities. In particular, the Home Owners Loan Corporation (HOLC) and the Federal Housing Administration (FHA) established public policies that contributed to racial market segmentation and racial segregation.

HOLC institutionalized redlining through its rating system developed allegedly to identify risk associated with making loans.<sup>7</sup> HOLC established four categories of neighborhood quality with the lowest category reserved for African American neighborhoods and color-coded red. The HOLC gave the highest rating to neighborhoods that were “new, homogenous, and in demand in good times and bad” and specified that these neighborhoods were to be occupied by “American business and professional men.” Although HOLC did not invent this system, it did place the full faith and credit of the United States behind the practice.

For decades, the FHA adopted HOLC ratings and the policies and practices that denied access to affordable mortgage products to African American borrowers. The FHA *Underwriting Manual* (1939) was crafted by Frederick Babcock, who wrote in his influential textbook *The Valuation of Real Estate* (1932) that “most of the variations and differences between people are slight and value declines are, as a result, gradual. But there is one difference in people, namely race, which can result in a very rapid decline. Usually such declines can be partially avoided by segregation and this device has always been in common usage in the South where white and negro populations have been separated.”<sup>8</sup> Babcock believed that “among the traits and characteristics of people which influence land values, racial heritage and tendencies seem to be of paramount importance. The aspirations, energies, and abilities of various groups in the composition of the population will determine the extent to which they develop the potential value of the land.”<sup>9</sup>

If only Babcock’s influence had ended with the FHA. Unfortunately, he is considered a seminal figure in the academic and practical application of real estate appraisal practices.<sup>10</sup> While African American veterans returning from World War II benefited from the educational benefits associated with the GI Bill and established the foundation of today’s African American middle class, Babcock’s influence denied them access to VA loan programs established under the Serviceman’s Readjustment Act of 1944.<sup>11</sup>

The FHA and VA loan programs made homeownership more than just a dream for the majority of Americans. Between 1934 and 1969, the home-ownership rate increased from 44 percent to 63 percent.<sup>12</sup> During this same period, less than one percent of all African Americans were able to obtain a mortgage.<sup>13</sup> During this period, the opportunity to create transgenerational wealth through homeownership was denied to minority households. As a result, white non-Hispanic households currently have a median net worth of \$79,400, including home equity, compared to \$7,500 for African American households.<sup>14</sup>

Thus, government failures encouraged and contributed to the racial wealth divide and the negative consequences it has had on my neighbors and my neighborhood. These decisions have benefited the majority at the expense of my community. This structural racism is a part of our national subconscious. Men like Babcock laid a foundation constructed on racial animus that has permeated our markets in ways that are as deadly and invisible as carbon monoxide.

Sadly, as we face the current mortgage credit crisis, we are repeating history through the adoption of “declining market” policies, the redefinition of credit risk in ways that continue the racial segmentation of our credit markets, and the assumption that the crisis was caused by providing access to credit to minority communities.

The explicit inclusion of race in the CRA offers us an opportunity to correct these government and market

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7 K. T. Jackson, *Crabgrass Frontier: The Suburbanization of the United States* (New York: Oxford University Press, 1985).

8 Frederick Babcock, *The Valuation of Real Estate* (New York: McGraw-Hill, 1932), 91.

9 *Ibid.*, 86.

10 N. Miller and S. Markosyan, “The Academic Roots and Evolution of Real Estate Appraisal,” *Appraisal Journal*, 71(2) (2003): 172–84.

11 38 U.S.C. §§ 3451.

12 D. S. Massey, “Origins of Economic Disparities: The Historical Role of Housing Segregation,” in *Segregation: The Rising Costs for America*, ed. J. H. Carr and N. K. Kutty (New York: Routledge, 2008), 39–80.

13 Reece, lectures at Kirwan Institute, 2008 (see note 6).

14 G. W. Domhoff, “Power in America: Wealth, Income, and Power,” from *Who Rules America?* Available at <http://sociology.ucsc.edu/whorules-america/power/wealth.html>.

failures, and would allow us to do more than just reduce the concentration of poverty and spatial isolation in neighborhoods of color. It would allow us to create opportunities for building real transgenerational wealth for minority families while protecting our nation's competitiveness in the global economy.

We have become painfully aware over the past few months that we live in a global society and the decisions we make have external costs and benefits far beyond our shores. If the United States is to remain globally competitive as we transition from the industrial to the information age, we cannot afford to leave communities of color behind. We must adopt strategies that will enable these communities to compete in the global marketplace by providing them with access to the capital they need for wealth creation and wealth retention in this new environment. Through a reimagining of the CRA, this can be accomplished through the support of both short-term and long-term strategies and market-based solutions.

## Policy Proposals

The CRA should explicitly reward financial institutions that aggressively engage in investments in minority wealth creation and minority neighborhood development.

Doing so would provide opportunities for all members of the community, and would begin to close the racial wealth divide that was created by twentieth-century government and market failures. We can close the divide by investing in programs that promote wealth creation, educational attainment, and sustained employment for minorities. Examples of these kinds of investments that promote wealth creation include: affordable homeownership programs; scholarships for higher education; work-study matching funds; paid internships for students attending historically black colleges and universities; and jobs that provide a living wage.

In addition to supporting minority wealth creation, this new twenty-first century market must support and empower minority neighborhoods with investments in neighborhood-based initiatives. Examples of these kinds of investments include: support for neighborhood redevelopment; the creation of neighborhood anchors such as major retail and grocery stores; financing housing and infrastructure; brownfield and vacant-property development; and support for minority small businesses

with technical assistance, affordable loans, and equity investments.

Through the CRA, we can promote public/private partnerships that encourage integrated and inclusive communities. These partnerships will develop initiatives that provide technical and public assistance in the design, packaging, and financing of neighborhood-based projects. These partnerships will promote employment opportunities for local residents and provide subcontracting opportunities for local minority and other community-based firms. The CRA can also be used to measure the extent to which banks do business with minority vendors, contractors, and professionals.

Explicitly including race in the CRA allows us to determine when, where, and how to effectively structure market interventions to correct past market failures. It allows us to develop strategies that challenge racial, social, and economic stratification by including a commitment to develop robust markets in minority communities. We must use the CRA and other public policy tools to correct market failures that support racial market segmentation and to create sustainable markets that are not dependent on the rationing of credit based on the observationally distinguishable characteristic of race. ■

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