Center for National Policy Review

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Mr. Alan R. Miller
Executive Secretary
Federal Deposit Insurance Corp.
550 17th Street, N.W.
Washington, D.C. 20429

Dear Sir:

The following comments on the proposed Fair Housing regulations published in the October 7, 1977 Federal Register are submitted by the Center for National Policy Review on behalf of itself and the organizations which were plaintiffs in National Urban League v. Office of the Comptroller.

General Comments

The proposed regulations constitute an essential first step in establishing the fair housing lending examination and enforcement program to which the FDIC is committed and which is called for by the Settlement Agreement in the Urban League case. The key element in that program is the collection and analysis of data concerning the race, sex and other characteristics of borrowers so as to identify patterns of potential discrimination at individual institutions. By collecting information on borrower creditworthiness, property characteristics, and loan terms, the system will be capable of controlling for factors, such as debt-to-income ratio, which are properly considered in loan decisions, thereby more accurately identifying lending patterns based on race or sex. In addition, by collecting data concerning factors which are often used in lending decisions but which are in fact discriminatory, such as age of dwelling, the proposed system will permit identification of institutions which appear to be using improper loan criteria.

While the proposed system is capable of producing a variety of useful analyses of lending patterns, the ultimate effectiveness of the enforcement program will depend on the work of the individual examiner. Hence examiner training and examination instructions are equally critical elements. Examiners will need to know how to search individual application and loan files for confirming signs and to question self-serving explanations of loan decisions by bank personnel. This is especially the case because it is proposed to draw only a sample of data from larger lenders, thus reducing the reliability of some of the analyses to be performed.

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The proposed regulations improve upon Regulation B's monitoring provision (12 CFR 202.13) in two important respects. First, the FDIC's proposal covers not only home purchase loans but also home construction, refinancing and improvement loans. Since race and sex discrimination are not limited to home purchase mortgages, the Regulation B limitation severely restricts the utility of its monitoring provision. The FDIC wisely proposes to monitor all forms of home financing loans.

A second major improvement is the FDIC's proposed requirement that race and sex data be collected on would-be borrowers who inquire about loans but do not reach the point of filing formal written applications. Discrimination in lending often takes the form of "pre-screening" would-be borrowers to whom bank officials do not wish to extend credit. Loan officers may quote onerous terms, or suggest that the likelihood of approval hardly justifies the payment of the application fee, or simply be "too busy" to return phone calls. If data collection is limited to those who file written applications, much discriminatory conduct will escape detection. Indeed, if lenders know that only written applications will be monitored, the incentive to "pre-screen" minority and female applicants will increase, and discrimination will not decline but simply occur earlier in the lending process.

The most serious deficiency in the FDIC's proposal is the absence of any elaboration on the broad non-discrimination requirements imposed upon banks by the Federal Fair Housing law and the Equal Credit Opportunity Act. As you know, the Federal Home Loan Bank Board has for some years had non-discrimination regulations and guidelines (21 C.F.R. 528 and 531.8) and has recently proposed substantial improvements in these rules (42 F.R. 58953, November 8, 1977). Now that the FDIC proposes to step up its fair housing lending enforcement activities, it is most important to provide similar guidance to its member banks and to the borrowing public. Therefore, we urge that the FDIC now prepare further proposed regulations on this subject.

Definitions (sec. 331.8)

"Inquirer." As stated above, a most important feature of the proposal is the requirement that race and sex data be collected on persons who inquire about loans but to do file written applications. This provision is responsive to concerns raised by the Urban League plaintiffs in their March, 1971 petition to the FDIC, asking that a "log of oral inquiries" be maintained at FDIC-member banks -- although as proposed, the regulation would omit telephonic inquiries.

The language of the proposal, however, may not clearly distinguish between mere "rate-shopping", in which the inquirer asks about current loan policies or terms without reference to a particular borrower or property, and more particularized inquiries in which information concerning the borrower or the property is given. It is the latter type of inquiry which may trigger discriminatory "pre-screening" based on borrower or property characteristics, and it would probably be useful to rephrase the definition of "inquirer" with this in mind. This might be accomplished by the following revision:

> (i) "Inquirer" means a natural person who makes a written or an oral in-person request for information about the terms of a home loan and furnishes any specific information concerning the inquirer or the dwelling, but who does not make application for such a loan.

We also propose that the definition of "inquirer" be extended to cover inquiries made on behalf of a would-be borrower by a broker or other person. In practice, inquiries are often made by brokers on behalf of their clients, and the exclusion of such inquiries from the proposed data collection system would rob it of much relevant data. This point could be covered by the following language:

> (i) "Inquirer" means a natural person who makes, or on whose behalf another person makes, a written or oral in-person request for information about the terms of a home loan, in which any specific information concerning the inquirer or the property is furnished but which is not followed by an application.

"Home mortgage loan." Although the proposed regulation evidently contemplates the inclusion of refinancing loans, this type of loan is not listed in the definition of "home mortgage loan." It seems desirable to expand the definition accordingly.

Equal Housing Lender Poster (sec. 338.3)

We welcome the changes made in the fair lending poster which banks are required to display, especially the listing of the FDIC as one of the agencies with which complaints may be filed. Indeed, we would prefer to see the FDIC listed ahead of the Department of Housing and Urban Development, because the Corporation's greater investigative resources and enforcement powers make it the more effective complaint-resolution agency.

We assume that the reference in the proposed poster to the "Office of Bank Customer Affairs" will be changed in the final regulation to the "Office of Consumer Affairs and Civil Rights."

Recordkeeping Requirements (sec. 338.4(a))

We have several specific comments on the recordkeeping requirements of sec. 338.4(a):

1. Paragraph (1)(v) calls for the address and Zip Code of property which is the subject of an "inquiry". The chief purpose for securing information concerning "inquiries" is to detect "pre-screening" of would-be borrowers, by comparing information concerning "inquirers" with similar information concerning "applicants." In order to detect discrimination based upon the racial characteristics of neighborhoods, the age of housing stock, or other improper neighborhood characteristics, it is most important that, wherever feasible,

geographic information include census tract. For this reason the Home Mortgage Disclosure Act requires census tract reporting, and paragraph (2)(ii)(C) calls for the census tract of property which is the subject of an application. Where feasible, property which is the subject of an "inquiry" should likewise be identified by census tract. Without this information, "pre-screening" of applicants from certain neighborhoods will escape detection, since there will not be an adequate basis for comparing "inquirer" with "applicant" information.

We realize that determination of census tract involves considerable effort on the part of lenders in some cases, but where the Federal Home Mortgage Disclosure Act or a state law or regulation would in any event require census tract determination this objection is eliminated. Accordingly, we urge that census tract be entered where Federal or state law would require this in the case of an approved loan.

2. With respect to paragraphs (2)(i)(F)(1) and (2), we note that "Liquid Assets" and "Assets which will be disposed of in connection with . . . the application" might be construed to cover the same assets and might result in duplicative reporting. For example, both terms might include savings account balances to be used for the down payment. These terms should be clarified to avoid possible overlap.

3. The phrase "terms which were considered appropriate at the last contact" in paragraph (2)(iii) seems unclear, since it does not indicate whether "considered appropriate" refers to the lender or the applicant. Perhaps the quoted language could be changed to read "terms which were offered by the institution at the last contact".

4. It is not clear why paragraph (5) does not require lenders to make available to examiners the information on "inquirers" required by paragraph (1) as well as the information "applicants" required by paragraphs (2) and (3). Examiners must be able to review information concerning "inquirers" and compare it with applicant information if they are to detect "pre-screening". A reference to paragraph (a)(1) should be added to the last sentence of paragraph (5).

5. We urge the addition of the property's appraised value to the items of information required by paragraph (2)(ii). Much of the discrimination which inhibits minority access to mortgage credit or which makes mortgage credit less available in minority, "changing" or older neighborhoods, stems from discriminatory appraisal practices rather than discriminatory underwriting policies. In order to detect discriminatory appraisals, it is necessary to compare appraised value with purchase price on a systematic basis, relating the comparison to the applicant's race and to the location of the property. This can only be done if lenders are required to report appraised value as well as purchase price.

Loan Officer Identification (sec. 338.4(b))

Completeness and accuracy of race and sex information is vital to the proposed data analysis program. Experience shows that many individuals do not provide personal information and that the proportion is higher among groups suffer-

ing a higher rejection rate -- presumably those subject to discrimination. Thus the provision requiring bank personnel to provide race/sex information where not supplied by the applicant or inquirer is most important. Experience with the 1974 Fair Housing Information Survey, Form C, in which loan officers supplied information not furnished by applicants, indicates that this requirement causes little difficulty.

We would, however, suggest an addition to the last sentence of section 338.4(b). That sentence calls on bank officials to provide missing data "from personal observation of the applicant or inquirer." We propose adding the words "or by reference to surname." Persons of Hispanic, Asian or American Indian descent may often be identified by surname.

Required information whose use may be improper

There are four items which lenders are required to record under section 338.4 (in addition to race, sex, marital status and age) whose use may be unlawful. These are (1) age of dwelling, (2) census tract or Zip Code, (3) customer or non-customer of bank, and (4) purchase price of property.

It is common to refuse to lend, under-appraise, or require more stringent terms on older dwellings or property in older neighborhoods. Not only does this practice have obvious and devastating effects on older urban neighborhoods, but since racial minorities disproportionately occupy these neighborhoods, the practice is racially discriminatory. The same comments apply to the common practice of refusing to lend or requiring stricter terms in certain neighborhoods because of their racial or ethnic composition. Likewise, some lenders refuse to make loans on property below an arbitrary value or purchase price, tending to make credit unavailable on smaller, older homes which, once again, are occupied by racial minorities in disproportionate numbers. Finally, while giving preference to customers of the bank may appear to be nothing more than sound business, where an institution has in the past discriminated against women or minorities, it perpetuates that discrimination by giving preferential treatment to its old customers. The data collection and analysis system should be designed to detect practices of this kind.

We assume, therefore, that the inclusion of these items among the information which lenders are required to report is, in part at least, intended to facilitate their isolation as factors in lending decisions, so as to permit follow-up by examiners. However, requiring banks to collect this information may lead them to suppose that its use is proper and is sanctioned by the FDIC. (Although race, sex, marital status and age are also required to be reported, lenders are presumably aware form the explicit terms of Federal statutes and regulations that consideration of these factors is illegal; the same is not true of the four factors under discussion.) It seems essential that lenders be forewarned, either by the regulation or by some other means, that use of these characteristics in lending decisions would in some circumstances be unlawful. Footnote 1 to section 338.4 is not sufficient to this prupose, since it could well be read to apply simply to the use of race, sex, marital status and age.

We believe that the proper way to deal with this matter is through the issuance of non-discrimination regulations or guidelines similar to those of the Federal Home Loan Bank, as urged in the last section of these comments. In the absence of such regulations, the four items referred to above should be footnoted to indicate that the use of this information may in some circumstances be unlawful, and that its inclusion in the regulation does not signify approval of such use by the FDIC.

Log Sheet

We urge two revisions in the log sheet included in the published proposal.

Column "M" provides for a lumping together of all minority groups, thus masking discriminatory patterns affecting only one of them. In practice, members of different minority groups may be treated differently. For example, blacks are often subjected to discrimination not affecting orientals, and Hispanic persons are subject to discrimination in some areas but not in others. In order to permit detection of "pre-screening" or application rejection patterns affecting only certain groups, lenders should be required to enter in the "M" column a letter symbol designating the inquirer's or applicant's racial identity.

In addition, in order to permit detection of "pre-screening" or application rejection patterns affecting particular neighborhoods, the log sheet should include a column for census tract or Zip Code.

Absence of non-discrimination regulations or guidelines

Although not required by the terms of the Urban League Settlement Agreement, the time has come for the FDIC to promulgate non-discrimination regulations similar to those recently proposed by the Federal Home Loan Bank Board. These should include a requirement that each bank have written underwriting and appraisal criteria and loan policies, an outline of appraisal and underwriting criteria whose effect is discriminatory and hence improper, and provisions to ensure that marketing practices and established broker and developer relationships do not have the effect of excluding minority group members from the lending services of the institution.

The Corporation's examination procedures require examiners to determine the lending policies of banks and determine whether they are in conformance with the fair lending laws. Without written statements of these policies, examiners must glean them from the self-serving, often vague and incomplete statements by bank personnel. Moreover, without clear written statements, it is most difficult for examiners to determine from loan files whether a bank's purported policies are consistently and fairly applied.

In addition, a written statement of appraisal and underwriting criteria would enable members of the borrowing public to assess their likelihood of securing mortgage credit and if so on what terms. It would also help them determine whether they were being dealt with fairly, thus reducing the number of ill-founded discrimination complaints against banks.

Lenders deserve guidance concerning the continued validity of appraisal and underwriting standards which have traditionally been used by banks. Neighborhood factors such as racial or ethnic composition, age of buildings, income level, and the like continue to influence lending decisions. So do stereotypic views of the creditworthiness of certain minorities and women. Personal history factors such as prior home ownership, credit difficulties from the distant past, arrest record, and educational level are considered in ways which adversely affect minorities and women despite absence of evidence relating these factors to creditworthiness, and with too little effort to determine their significance in the case of the individual applicant. Lenders and borrowers deserve guidance concerning the propriety and legality of these practices in light of current laws and current views of the obligations of regulated lenders to their communities.

The marketing practices and business relationships of banks will come under review pursuant to the Community Reinvestment Act. But, as the FHLBB's proposed guidelines recognize, business policies and relationships whose effect is to restrict lending opportunities to a predominantly white or predominantly male clientele violate the Fair Housing and Equal Credit Opportunity Acts. Included in these practices would be giving preference to old customers, in cases where prior banking practices have been exclusionary. Again, lending institutions subject to FDIC supervision deserve some guidance on these matters.

This is not the place to discuss the details of the needed non-discrimination regulations. But it is our view that the FDIC's new examination and enforcement program requires a better yardstick against which to measure compliance than the rather general language of the statutes which the Corporation enforces.

Sincerely yours,

Roger S. Kuhn

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