REINVESTMENT ALERT

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PROPOSED COMMUNITY REINVESTMENT ACT TESTS SHOW LARGE MORTGAGE COMPANIES LACKING

The New CRA Rules

New lending tests proposed by federal bank regulators show that some large Chicago area mortgage companies have poor lending records in low- and moderate-income neighborhoods. The lending tests are part of the new regulations proposed under the Community Reinvestment Act (CRA). The CRA was passed by Congress in 1977 to combat redlining and lending discrimination by banks and savings and loans. Mortgage companies are not subject to the Community Reinvestment Act. The large mortgage companies' poor showing suggests it is time they too were included under the Community Reinvestment Act.

President Clinton, as part of his bank regulatory reform agenda, has asked federal regulators to revisit the CRA to make it more effective. The changes proposed by federal regulators would move CRA examinations from a concentration on process and paper work to an emphasis on financial institutions' patterns of lending in lower income communities.

The proposed regulations provide for three types of tests: (1) tests of banks' lending patterns in their service area (the lending test); (2) a measure of banks' lending to low- and moderate-income neighborhoods and individuals through intermediaries such as community development corporations (the investment test), and (3) an examination of whether a retail bank has branches that are in, or readily accessible to, low- and moderate-income neighborhoods (the service test).

Since late December, when the proposed changes were made public, community groups and lenders around the country have engaged in a vigorous debate over the appropriateness of the new measures. As part of this debate, the Woodstock Institute has performed an analysis of how some of the largest banks and mortgage companies operating in Cook County would perform under the new lending tests.

The Woodstock Institute Analysis

In order to perform a timely analysis of the lending tests, the Woodstock Institute decided to look only at the lending patterns of five large depository institutions that included all of Cook County in their service areas and the five mortgage companies with the largest number of loans in Cook County. (The five depository institutions account for 14,857 loans to low- and moderate-income tracts in Cook County which is nearly 14 percent of all the loans to those tracts. The top five mortgage companies made 5,622 loans to these lower income neighborhoods or 13 percent of all loans made by nondepository institutions.)

Under the proposed lending test, a financial institution's lending patterns would be examined for the whole of its service area. Mortgage companies have no defined service areas, and some of the larger banks have service areas larger than Cook County.

"Using Cook County was a choice we made to insure that community groups and financial institutions could benefit from this analysis before the March 24 deadline for comment on the changes passed," said Woodstock President Malcolm Bush. "If anything, reducing the service area to Cook County only made some institutions look better on the lending tests than they otherwise would have," remarked Vice President Dan Immergluck. "A bank's performance on these tests is likely to decline as you include middle income counties in the test." Bush added that mortgage companies were included in the analysis because they were large lenders and because it was time they were subject to CRA examinations. This analysis does not include commercial and personal loans because data on these loans are not yet available. Commercial and personal lending will also be examined in the new CRA process.

Market Share Analysis

The first of the proposed lending tests examines a financial institution's market share of lending in low- and moderate-income neighborhoods compared to the same institution's market share in all other neighborhoods. The test presumes that a financial institution which is living up to its legal obligation to lend throughout its service area will have a similar market share in both groups of neighborhoods. The new test will examine separately housing, business and personal loans. The Woodstock Institute analysis includes the housing loans of five large depository institutions operating throughout Cook County and five large mortgage banks using Home Mortgage Disclosure Act (HMDA) data.

Table I shows the ratio of each financial institution's market share of low- and moderate-income census tracts with their market share in all other census tracts in Cook County. It is a summary of Table II which describes how the ratio was calculated.

Ratios over 1.0 such as the Harris Bank ratio, indicate that a financial institution has a larger market share of the low-mod census tracts than it does of non-low- mod census tracts. Institutions with such high numbers will get better CRA grades. In order to get an outstanding rating on the lending test, a bank's share of loans in low- and moderate-income neighborhoods must "significantly exceed its market

TABLE I
Market Share Summary (1992 Data)

Banks and Savings and Loan	Market Share Ratio*	Mortgage Companies	Market Share Ratio**
First National Bank of Chicago	.96	Countrywide Funding Corp.	.34
The Northern Trust Company	.65	Crown Mortgage Company	.45
Harris Trust and Savings	1.11	Margaretten and Company	1.67
LaSalle Talman FSB	.91	NBD Mortgage Company	.24
St. Paul Federal	.82	Sears Mortgage Company	.52

* Market=All Banks and Savings and Loans
** Market=All Mortgage Companies

share of reportable loans in the rest of its service area." For the banks and savings and loans chosen for this study, ratios range from 0.65 to 1.11.

While one mortgage company, Margaretten, outperforms all banks and savings and loans with a ratio of 1.67, the four other major mortgage companies ratios range between 0.23 and 0.52. Such low numbers suggest that these mortgage companies are not serving low- and mod-income communities adequately. The new regulations state that a financial institution would get a substantial non-compliance rating on the lending test if its market share in low- and moderate-income neighborhoods "is significantly less than its market share of reportable loans in the remainder of its service area".

The five large mortgage companies account for 34 percent of all mortgage company loans in Cook County. Even though some mortgage companies do substantial lending in lower income neighborhoods, many are heavy users of FHA loans and there are problems associated with the misuse of FHA loans including high default and foreclosure rates in some communities.

Distribution of Loans Analysis

Another proposed lending test, the distribution test, looks at the percent of lower income census tracts in which a bank makes loans. The purpose of the distribution test is to ensure that bank lending is geographically spread throughout the bank's service area.

TABLE II
CRA Proposal Analysis
Market Share Test--Cook County Only (1992 Data)

Lender	Lender Type	Total Loans	# of Loans in Low-Mod Census Tracts	# of Loans in All Other Census Tracts	A Market Share* in Low-Mod Census Tracts	B Market Share** in All Other Census Tracts	A/B Market Share Ratio (Column A Divided By Column B)
First National Bank of Chicago	Bank	5,629	745	4,884	5.0%	5.2%	0.96
The Northern Trust Company	Bank	1,825	170	1,655	1.1%	1.8%	0.65
Harris Trust and Savings	Bank	851	127	724	0.9%	0.8%	1.11
LaSalle Talman FSB	S&L	9,192	1,154	8,038	7.8%	8.6%	0.91
St. Paul Federal	S&L	2,278	263	2,015	1.8%	2.1%	0.82
All Banks and Savings and Loans		**108,672**	**14,857**	**93,815**	**100.0%**	**100.0%**	

* # of loans as a percentage of all loans made by banks and savings and loans in low-mod census tracts in Cook County
** # of loans as a percentage of all loans made by banks and savings and loans in all other census tracts in Cook County

Lender	Lender Type	Total Loans	# of Loans in Low-Mod Census Tracts	# of Loans in All Other Census Tracts	A Market Share* in Low-Mod Census Tracts	B Market Share** in All Other Census Tracts	A/B Market Share Ratio (Column A Divided By Column B)
Countrywide Funding Corp.	Mort. Co	2,145	105	2,040	1.9%	5.5%	0.34
Crown Mortgage Company	Mort. Co	2,154	138	2,016	2.5%	5.4%	0.45
Margaretten and Company	Mort. Co	5,212	1,054	4,158	18.7%	11.2%	1.67
NBD Mortgage Company	Mort. Co	2,817	98	2,719	1.7%	7.3%	0.24
Sears Mortgage Company	Mort. Co	2,077	152	1,925	2.7%	5.2%	0.52
All Mortgage Companies		**42,771**	**5,622**	**37,149**	**100.0%**	**100.0%**	

* # of loans as a percentage of all loans made by mortgage bankers in low-mod census tracts in Cook County
** # of loans as a percentage of all loans made by mortgage bankers in all other census tracts in Cook County

# of Low-Mod Census Tracts in Cook County	586
# of All Other Census Tracts in Cook County	743
# of Census Tracts Income Level Unknown in Cook County	23

TABLE III
CRA Proposal Analysis
Composition and Distribution -- Cook County Only

Lender	Lend Type	Total Loans	# of Loans in Low-Mod Census Tracts	# of Loans in All Other Census Tracts	% of Loans in Low-Mod Census Tracts	# of Cook County Low-Mod Census Tracts Where Lender Has Made: 1+ Loans	% of Cook County Low-Mod Census Tracts Where Lender Has Made: 1+ Loans
First National Bank of Chicago	Bank	5,629	745	4,884	13.2%	294	50.2%
The Northern Trust Company	Bank	1,825	170	1,655	9.3%	122	20.8%
Harris Trust and Savings	Bank	851	127	724	14.9%	85	14.5%
LaSalle Talman FSB	S&L	9,192	1,154	8,038	12.6%	322	54.9%
St. Paul Federal	S&L	2,278	263	2,015	11.5%	143	24.4%
All Banks and Savings and Loans		**108,672**	**14,857**	**93,815**	13.7%		
Countrywide Funding Corp.	Mort.	2,145	105	2,040	4.9%	61	10.4%
Crown Mortgage Company	Mort.	2,154	138	2,016	6.4%	97	16.6%
Margaretten and Company	Mort.	5,212	1,054	4,158	20.2%	269	45.9%
NBD Mortgage Company	Mort.	2,817	98	2,719	3.5%	58	9.9%
Sears Mortgage Company	Mort.	2,077	152	1,925	7.3%	71	12.1%
All Mortgage Companies		**42,771**	**5,622**	**37,149**	13.1%		
# of Low-Mod Census Tracts in Cook Count			586				
# of All Other Census Tracts in Cook County			743				
# of Census Tracts Income Level Unknown in Cook County			23				

The last column in Table III shows the percentage of the 586 low- and moderate-income census tracts in Cook County in which each financial institution makes loans. For banks and savings and loans the numbers range from a low of 14 percent of census tracts for Harris to a high of 55 percent for LaSalle. The corresponding figures for the mortgage companies are between 10 percent for NBD and 46 percent for Margaretten, with all but one of the mortgage companies lending in fewer than 17 percent of lower income census tracts in Cook County. Larger institutions would be expected to lend in a larger number of census tracts, and so are likely to do better when compared to smaller lenders in the same geographic areas.

Concentration of Loans Analysis

The proposed new regulations include an alternative to measuring the percent of lower income census tract where a bank extends loans. Financial institutions can choose instead to measure the percent of all their loans that go to lower income tracts. This test rewards banks which concentrate their lower income lending in a smaller number of tracts thereby having a greater chance of boosting economic activity in those neighborhoods.

Table III shows that four out of five depositories have between 11 and 15 percent of their loans in lower income neighborhoods, while four out of five mortgage companies have between 3 and 7 percent of their loans in those neighborhoods.

Conclusion

The new lending tests in CRA examinations would give banks and community groups a much clearer picture of financial institutions' lending effort in modest income neighborhoods. The use of several indicators of bank performance gives a more accurate picture than the use of any one measure. Banks which perform badly on one test may well perform well on another, and only the examination of several figures give a full picture of lending activity. Malcolm Bush commented that this analysis shows the importance of the proposed regulations. "For the first time," he said, "we will know whether a lending institution is pulling its weight."

The disparity between the large depository institutions and mortgage companies' lending activity is clear evidence for the need to include mortgage companies under the Community Reinvestment Act. Community reinvestment activity is too critical to the health of urban areas to omit mortgage companies from federal examination. While the Illinois Commissioner of Savings and Residential Finance examines mortgage companies, state examination of community reinvestment activity is a pale shadow of the examinations conducted by federal regulators.