

In Election's Aftermath, CRA Stays a Flash Point

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WASHINGTON — The debate on whether the Community Reinvestment Act caused the subprime crisis has outlasted election season and could affect future regulatory restructuring.

Though there is scant evidence and growing dissent from regulators, Republican lawmakers appear poised to make CRA a fall guy for the financial meltdown, arguing that it spurred banks to make poor loans that eventually led to delinquencies and foreclosures. Some said they plan to tackle the issue next year as Congress works to revamp the broader regulatory structure.

"The overwhelming support" in the Republican party "is for changing the CRA," Rep. [Scott Garrett](#), R-N.J., a member of the [House Financial Services Committee](#), said in an interview. "It's high on the agenda as far as trying to fix the entire collection of regulations that exacerbated the housing bubble."

Rep. [Jeb Hensarling](#), R-Tex., also argues that the financial services panel should "explore the role the CRA played in exacerbating the subprime meltdown and figure out how much bad lending was done in order to fulfill CRA goals," a spokesman said.

Regulators, even Republican ones, are beginning to push back.

Both Federal Reserve Board Governor [Randall Kroszner](#) and Comptroller of the Currency John Dugan have recently expressed strong support for the CRA.

In an interview Wednesday, Mr. Dugan said he felt obliged to speak up against criticism of CRA. Data does not support the idea that bankers made poor loans as a result of such requirements, he said.

"There has been criticism recently suggesting that the CRA caused the subprime crisis, and we just felt it was important to set the record straight because that's not what we saw," he said.

After a speech on the subject last month, Mr. Dugan was hailed by House Financial Services Committee Chairman [Barney Frank](#) in a speech on the House floor. "This firm statement by President Bush's appointee with prime responsibility for the safety and soundness of the banking system should help us end the inaccurate, politically motivated misrepresentation of the role that CRA has played," he said.

Critics of the CRA have argued that the law, passed in 1977 to combat discrimination by banks against poor and minority communities, forces banks to lend to borrowers who are poor credit risks. They say CRA regulations have caused lenders to lower their underwriting standards.

"It caused standards for mortgages to deteriorate very substantially because it forced banks to find new ways to offer mortgages to people who couldn't meet the normal standards," said [Peter Wallison](#), a fellow at the [American Enterprise Institute](#) and a member of the [Shadow Financial Regulatory Committee](#). "Then

those lower standards spread to the rest of the mortgage markets, so people who could have qualified for prime loans were able to get interest-only or negative amortization loans, and all of those things became more or less the standard for mortgage loans."

Mr. Wallison argued that the CRA should be scrapped.

But others said the focus on CRA is a red herring. They said it is a talking point for Republicans who want to distract attention from a growing consensus that more regulation is needed.

"I think that the deregulatory conservatives have a political motivation in trying to deflect attention from the underlying causes of the subprime and financial crisis to anything they can find, including the CRA," said [Michael Barr](#), a law professor at the [University of Michigan](#) who has testified to Congress on the CRA's reputed role in the subprime crisis. "The facts just don't support the claim. The overwhelming bulk of subprime lending was made by institutions not covered in the CRA."

Mr. Kroszner on Wednesday told an audience attending a Fed conference on poverty policy that the CRA had not caused lenders to make a significant number of bad loans. He reviewed studies by the Fed showing that CRA lending was "nearly as profitable and performed similarly to other types of lending done by CRA-covered institutions." The Fed's most recent mortgage study showed that 60% of high-priced loans went to middle- or upper-income borrowers, those outside the CRA's target population, and that 20% of high-priced loans to low-income borrowers were not made by banks, he said. Instead, they were made by nonbank lenders not bound by the CRA.

"Contrary to the assertions of critics, the evidence does not support the view that the CRA contributed in any substantial way to the crisis in the subprime mortgage market," Mr. Kroszner said.

Some bankers clearly agree.

During a panel discussion Wednesday at the [Charlotte Chamber of Commerce](#), [Ken Lewis](#), [Bank of America Corp.](#)'s chief executive officer, said CRA has become a "scapegoat" for the current mortgage crisis.

"The great majority of loans that caused this problem were outside of CRA," he said.

Given Democrats' control of Congress and the White House, Republicans have little chance of prevailing on CRA in the near term. But some observers said the focus on CRA is meant to lay the groundwork for change later.

"Changes in regulatory laws happen through people stating their case as to why things work or don't work," said [Douglas Landy](#), a partner at [Allen & Overy LLP](#).

"Those arguments are batted back and forth for years — or even decades. So people put in their place holders. You're not sure exactly when an idea is going to come back."

That has in turn spurred regulators to respond, Mr. Landy said.

"I think the Fed, as one of the regulators that enforces the CRA and perhaps as the primary regulator that enforces consumer finance rules, wants to set the record straight," he said.

Mr. Barr, the Michigan law professor, said the attempt to divert the attention of participants in the regulatory reform debate appeared to be failing, despite the recent attention from regulators.

"I think that it has failed so far because it's implausible on its face, the facts don't support it, and the country as a whole recognizes the origins of our crisis were in a failure of government to act and not in the CRA," Mr. Barr said.