



MORTGAGE BANKERS ASSOCIATION

Applying CRA to Independent Mortgage Banks: An Ineffective and Misguided Policy Choice

<i>Issue:</i>	Regulators and legislators – at both the federal and state levels – are considering options to extend the reach of the Community Reinvestment Act to independent mortgage banks.
<i>Concern:</i>	These policy options represent a solution in search of a problem and do not recognize the incompatibility of the Community Reinvestment Act with the business models and historical lending activities of independent mortgage banks.
<i>Highlights:</i>	Independent mortgage banks: <ul style="list-style-type: none">• Do not have deposits to reinvest• Do not have access to direct government support• Engage in sustainable lending in low- to moderate-income communities• Are subject to robust oversight and supervision
<i>Bottom Line:</i>	The application of the Community Reinvestment Act to independent mortgage banks would be an ineffective and misguided policy choice.

In recent months, regulators, legislators, and others in the public policy community have re-visited the structure and contours of the Community Reinvestment Act (CRA; Act). The CRA was enacted in 1977 to encourage covered depository institutions to “demonstrate that their deposit facilities serve the convenience and needs of the communities in which they are chartered to do business,” including “the need for credit services as well as deposit services.”¹ While various amendments to the implementing regulations have been made over the past 40 years, major changes in the nature and provision of financial services have spurred some to call for more fundamental CRA modernization efforts.

Among the options being considered by Congress and state legislatures is an expansion of CRA requirements to apply to non-depository lenders, such as independent mortgage banks (IMBs). This would be a major policy mistake—one that overlooks the data on IMB performance in serving low- to moderate-income (LMI) communities and rests on a misunderstanding of the IMB business model as well as the purposes of the CRA.

¹ 12 U.S.C. § 2901(a).

Lack of Deposits to Reinvest

The CRA was designed to cover deposit-taking institutions that enjoy the benefits of federal deposit insurance provided by the Federal Deposit Insurance Corporation (FDIC). These institutions include national banks, savings associations, and state-chartered commercial and savings banks. The primary purpose of the Act is to ensure that if financial institutions accept deposits from a particular community or population, they also lend to, or invest in programs or activities that benefit, that community or population. In other words, in exchange for receiving FDIC deposit insurance, these institutions must *reinvest* an appropriate proportion of these deposits in a fair and equitable manner—hence, the name of the Act.

In contrast to FDIC-insured institutions, IMBs do not accept deposits from their customers as a source of funds to lend or invest, and therefore are not recipients of FDIC deposit insurance. IMBs instead use short-term borrowing, or warehouse lines of credit, to obtain the funds needed to originate mortgages. This borrowing is secured by the funded mortgages until the mortgages are sold to investors in the secondary market. As a result, the IMB business model is designed to *import* funds from global capital markets and lend those funds in local communities to support homeownership. IMBs do not take in deposits or other resources from these local communities, and therefore the concept of *reinvesting* does not apply. Rather, IMBs channel capital from outside the local community into productive uses within that community. At its core, this is an entirely different model of originating mortgages than the model used by banks, and it is not compatible with the requirements of the CRA.

Lack of Access to Direct Government Support

The CRA obligations imposed on banks not only represent a policy choice to promote lending and investing in LMI communities, but also are a mechanism to ensure that institutions receiving access to various types of government support serve the taxpayers that provide this support. Many depository institutions that are subject to the CRA, for example, are eligible to access deposit insurance from the FDIC, advances from the Federal Home Loan Banks (FHLBs), and emergency loans from the Federal Reserve through the discount window. These programs provide both reliable liquidity on an ongoing basis and backstop funding in periods of stress.

IMBs, however, are ineligible for any of these government benefits. If an IMB faces liquidity strains, it cannot turn to FHLB advances or obtain funding from the Federal Reserve discount window. The operations of IMBs are not directly supported by federal backstops in the way that is true of insured depository institutions' operations. As such, imposing CRA obligations on IMBs as a means of compensating taxpayers imposes cost burdens on IMBs with no offsetting benefits.

Robust Lending in LMI Communities

One of the main objectives of the CRA is to ensure reliable, sustainable lending to LMI borrowers and communities throughout the country. This is a laudable goal, and any national housing policy should foster and promote such lending. Those arguing to extend CRA obligations to IMBs on these grounds often ignore the fact that IMBs already engage in substantial lending in LMI communities—and IMBs compare very favorably to other types of financial institutions in this regard.

Based on Home Mortgage Disclosure Act (HMDA) data and the CRA files from the Federal Financial Institutions Examination Council (FFIEC), the Urban Institute found that IMBs have a higher LMI borrower share and LMI area share than banks, whether viewed by loan count or dollar volume.² Similarly, IMBs are the dominant originators in the government housing finance programs operated by the Federal Housing Administration (FHA), Department of Veterans Affairs (VA), and Rural Housing Service (RHS). The FHA program, in particular, primarily serves LMI borrowers and accounts for a disproportionate share of lending to minority borrowers and first-time homebuyers. According to 2019 HMDA data, IMBs originated more than 85 percent of FHA loans, 74 percent of VA loans, and 69 percent of RHS loans. Further, IMBs originated nearly 67 percent of loans to minority borrowers and approximately 62 percent of purchase loans for LMI borrowers. Finally, IMBs served homebuyers with lower average purchase loan amounts (\$264,000) than their depository counterparts (\$298,000).³

Taken together, these statistics point to a clear conclusion—IMBs do not need any regulatory obligation or incentive in order to serve LMI borrowers and communities; they have a strong history of doing so that continues today. As a result, extending CRA coverage to IMBs is very much a policy solution that is detached from IMBs' willingness and ability to provide mortgage credit to LMI borrowers and communities.

Strengthened Regulatory Oversight

Another argument made in favor of a broader CRA that applies to IMBs centers on the idea that CRA examinations serve as a defense against poor underwriting practices, such as those that were prevalent in some areas of the mortgage market in the years prior to the financial crisis. As this argument goes, IMBs that do not undergo bank examinations would be well served to submit to CRA examinations to better ensure that the loans they originate are sustainable for consumers.

This view, however, is rooted in a pre-2008 regulatory framework and ignores the dramatic changes in both the state and federal oversight of IMBs over the past decade.

² Goodman, Laurie, Jun Zhu, and John Walsh, "The Community Reinvestment Act: Lending Data Highlights," Urban Institute, November 2018. Available at: https://www.urban.org/sites/default/files/publication/99427/community_reinvestment_act_lending_data_highlights_update.pdf.

³ Mortgage Bankers Association, "Independent Mortgage Banks: Financing the American Dream." Available at: https://www.mba.org/Documents/Policy/22153_MBA_IMB_Summary_Report_2021.pdf.

In addition to more robust prudential standards that are applied by state regulators and counterparty risk standards that are applied by Fannie Mae, Freddie Mac, Ginnie Mae, and warehouse lenders, IMBs also are subject to the supervisory, investigative, and enforcement authority of the Consumer Financial Protection Bureau (CFPB). The CFPB examines IMBs with respect to their lending practices and their compliance with consumer-facing regulations.

Further, the regulatory framework in place in the mortgage market today effectively has eliminated the damaging types of products that contributed to the financial crisis—for lenders of all types. The CFPB’s ability-to-repay rules and the accompanying Qualified Mortgage standard, for example, better ensure thorough documentation of borrower income, assets, employment, and debt, as well as promote product features that are more likely to foster long-term homeownership for consumers.

In contrast, CRA examinations are not the mechanism by which to ensure high-quality lending. Such an argument conflates the purpose of the CRA and fails to recognize the far-superior post-crisis methods for overseeing underwriting practices that now are in place for all lenders. Again, the CRA simply is the wrong solution to the concerns raised in this context.

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National housing policy can and should seek to ensure that LMI borrowers and communities have access to mortgage credit on a fair and equitable basis. Indeed, all lenders should serve such borrowers and communities, and discrimination in any form should not be tolerated. The CRA is a vital component of this policy objective, though advocates of extending CRA to IMBs should remember that the CRA has a far more specific purpose. The CRA is meant to ensure that financial institutions accepting deposits from a particular community or population reinvest those deposits in that community or population.

IMBs do not accept deposits, nor are they the beneficiaries of direct taxpayer backstops for their ongoing operations. They have a proven track record of strong and reliable lending to LMI borrowers and communities, and are subject to the same consumer-facing regulations as depository institutions, which ensures sound underwriting and high-quality lending.

Subjecting IMBs to the CRA therefore would impose costs on IMBs that are unlikely to produce significant incremental benefits, given the important role IMBs already play in serving LMI borrowers. As such, CRA is an ineffective and misguided policy choice with respect to IMBs—a mistake that Congress and state legislatures should take care to avoid.