

The Home Mortgage Disclosure Act: Its History, Evolution, and Limitations

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This paper analyzes the history of the Home Mortgage Disclosure Act (“HMDA”). It focuses on the general purposes of HMDA and the evolution and expansion of those purposes over time. Finally, it discusses the limitations of the data in determining whether discrimination has occurred.

I. History of HMDA

The history of HMDA since it was enacted in 1975 can be divided into three major phases, reflecting the dramatic changes in the mortgage industry that have occurred since enactment, as well as changes in perception by the industry’s critics in the advocacy community and on Capitol Hill regarding how the industry serves low-income communities and members of minority groups.

- **Depository institution community reinvestment/disinvestment model.** From enactment until the late 1980s, HMDA reporting focused on originations by depository institutions in urban areas. This reflected the perception that banks and thrifts were taking deposits from lower-income neighborhoods but not “reinvesting” that money in the form of loans to the same neighborhoods. No application data were collected, and HMDA reporting did not include racial or ethnic data about particular borrowers. Institutions reported aggregate statistics about dollar amount and specific location of their residential loans but did not have to disclose their lending on a loan-by-loan basis. HMDA data were expected to assist regulators in identifying institutions that were failing to lend money in communities in which they were taking deposits and to help local officials identify neighborhoods that were not receiving sufficient capital to stem urban decay.
- **Mortgage lender discrimination model.** Starting in the late 1970s, mortgage lending began to migrate from traditional depository institutions that hold loans in portfolio to non-bank mortgage bankers (including affiliates of banks and thrifts), often operating on a regional or nationwide basis, that would sell loans into the secondary market. The model of a mortgage market provided by community banks that make local mortgage loans funded by local deposits began to fade (although it still has not entirely disappeared), as did the notion that

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lenders were engaging in wholesale redlining of neighborhoods, as opposed to more subtle forms of discrimination. By the mid- to late-1980s, advocates and government regulators had begun turning their attention to the lending practices of the new types of mortgage lenders. The focus changed from “disinvestment” in certain neighborhoods to discrimination in underwriting. As a result of legislative changes in the late 1980s, HMDA reporting was vastly expanded. It now included data about most bank and non-bank lenders in urban areas. The data now included racial, ethnic, and gender information, as well as income for each applicant, and reflected both rejected and accepted applications for loans that did not close. In implementing the legislative changes, the Federal Reserve Board (“FRB” or “Board”) decided to require public disclosure of each application and closed loan, with identifying information redacted.

While the expanded HMDA data showed that most institutions accepted the vast majority of applications from any group, they also showed a disparity in the acceptance rates between groups, and in particular, higher acceptance rates for whites than either African-Americans or Hispanics. Some community advocates immediately equated these disparities with discrimination, although the HMDA data still omitted much of the information considered in mortgage underwriting, including such critical factors as the applicant’s credit history and current debt load. The Federal Reserve Bank of Boston conducted a study (the “Boston Fed Study”) that augmented the HMDA data with other underwriting information. The conclusion of that study was that there was a smaller but still real disparity between white and minority rejection rates even after controlling for legitimate underwriting factors. Both scholars and the lending industry vigorously disputed that finding, criticizing both the design and the execution of the Boston Fed Study. At the same time, lenders responded to the findings by making their underwriting criteria more flexible and convincing the largest government-sponsored enterprises (“GSEs”), Fannie Mae and Freddie Mac, to do the same. Lenders also created new products that were tailored to lower-income borrowers and increased their outreach efforts. Bank regulators began to use HMDA data, especially denial-disparity ratios, to identify institutions on which they would focus fair lending examination efforts. These efforts led to several Department of Justice investigations and enforcement actions. Community activists used analyses of individual institutions’ HMDA data in attempts to stall bank mergers, bring negative publicity to those institutions, or obtain lending commitments from the institutions.

- **Predatory lending/price discrimination model.** One result of lenders’ efforts to respond to the expanded HMDA reporting and the studies growing out of it was that fewer applicants were rejected outright for credit. Instead, with a growing range of products and terms available, many more borrowers were offered loans. At the same time, nonprime lending in general was growing rapidly and a secondary market for nonprime loans developed. Although these changes gave many more people access to financing to purchase and maintain their homes, the growth of this market was accompanied by complaints from community advocates of “predatory lending.” In addition, with fewer applicants being rejected, the HMDA data about accepted and rejected loans were becoming less meaningful, and advocates claimed that lenders were offering credit to minorities and lower-income communities but on less favorable terms. In response, the FRB amended HMDA’s implementing Regulation C to require reporting of pricing and Home Ownership and Equity Protection Act (“HOEPA”) status on loans above a given price threshold. In an effort to

improve the quality of HMDA data, the revised regulation also tightened the definitions of different types of loans and required the collection of racial and ethnic monitoring information in telephone applications.

HMDA Today: Current Requirements

Before recounting the history of HMDA, it is useful to summarize what the law currently requires. HMDA is implemented by the FRB in Regulation C.¹ HMDA's main features include the following:

- **Coverage.** HMDA has two categories of coverage: depository institutions (banks, credit unions, and savings associations) and other mortgage lenders. A depository institution is covered if it:
 - Had assets of more than \$34 million on the preceding December 31;
 - Had a home or branch office in a metropolitan area² on the preceding December 31;
 - In the preceding calendar year, originated at least one home purchase loan or refinancing of a home purchase loan secured by a first lien on a one-to-four-family dwelling; and
 - Either is federally insured or regulated, or originated a home purchase loan or refinancing that was insured, guaranteed, or supplemented by a federal agency.

A mortgage lender other than a depository institution is covered if:

- It is a for-profit lender;
 - In the preceding calendar year, its home-purchase loan originations (including refinancings of home-purchase loans), measured in dollars, were either 10% or more of its total loan originations or \$25 million or more;
 - It had a home or branch office in a metropolitan area on the preceding December 31, or received applications for, originated, or purchased five or more home-purchase (including refinancings) or home-improvement loans on property located in a metropolitan area in the preceding calendar year; and
 - It had assets (including the assets of any parent corporation) of more than \$10 million on the preceding December 31, or originated 100 or more home purchase loans (including refinancings of home purchase loans) in the preceding calendar year.
- **Data reporting.** Covered lenders must compile data in a Loan/Application Register (“LAR”) about applications for, originations of, and purchases of home-purchase loans,

¹ 12 C.F.R. part 203.

² HMDA has always required reporting of lending in metropolitan areas, although the terminology used to describe those areas has changed over time. The current terminology is “metropolitan statistical area or metropolitan division.” This paper will refer to areas subject to HMDA reporting as “metropolitan areas.”

home-improvement loans, and refinancings of home-purchase loans. They may also report home-equity lines of credit opened wholly or partly for home-improvement or home-purchase purposes. The following information must be collected for each application or loan:³

- An identification number for the application or loan.
- The date the application was received.
- The type of loan (conventional, government-guaranteed, or government-insured). Government loans are identified by the insuring or guaranteeing agency.
- The property type (1-4 family dwelling [including condominiums and co-ops], manufactured housing, or multifamily dwelling).
- The purpose of the loan (home purchase, home improvement, or refinancing).
- Occupancy (whether a 1-4 family dwelling, including a manufactured home, is the borrower's principal dwelling). This information is optional for multifamily dwellings and for those located outside metropolitan areas or in metropolitan areas where the lender does not have a home or branch offices. On a purchased loan, the lender can assume that the property is owner-occupied unless the application or loan documents indicate otherwise.
- The loan amount, in thousands of dollars. For purchased loans, this field is the balance at time of purchase.
- Whether the loan was initiated as a "preapproval request," defined as a request for a written, time-limited commitment to make a loan that is subject only to finding an acceptable property and typical closing conditions. This field does not apply to purchased loans.
- The action taken on the loan (loan originated, application approved by the lender but not accepted by consumer [*i.e.*, withdrawn after approval by lender], application denied, application withdrawn, file closed for incompleteness, preapproval request denied, or preapproval request approved but not accepted [reporting approved but not accepted preapproval requests is optional]). Purchased loans are simply reported as loans purchased by the institution.
- The date the action was taken.
- The location of the property, including identification of the metropolitan area, the state and county, and the census tract. The census tract may be omitted if the property is located in a county with a population of 30,000 or less as of the 2000 census. Location information may be omitted entirely if the property is located outside a metropolitan area in which the lender has a home or branch office, or outside any metropolitan area, unless

³ See 12 C.F.R. part 203 app. A.

the lender is required to report under the Community Reinvestment Act (“CRA”). It may also be omitted if a preapproval request was denied, or approved but not accepted by the applicant.

- Race, ethnicity (Hispanic or not Hispanic), and sex of the applicant and co-applicant (if any), for both loans that were originated and loan applications that did not result in an origination. Reporting this information is optional for purchased loans.
- Applicant’s income in thousands of dollars (defined as the income that the institution relied on in making its credit decision).
- The type of purchaser. This field applies only to loans sold into the secondary market in the same calendar year that they were originated or purchased. Lenders must report the type of purchaser, such as Fannie Mae; Freddie Mac; Ginnie Mae; a private securitization; a commercial bank or thrift; an insurance company, credit union, mortgage bank, or finance company; or an affiliated institution.
- Up to three reasons for denial. This is an optional field, except that institutions that are supervised by the Office of Thrift Supervision (“OTS”) or Office of the Comptroller of the Currency (“OCC”) must include it under those agencies’ regulations.⁴
- Rate spread. Lenders must report interest-rate information on certain home purchase loans, refinancings, or home improvement loans secured by a dwelling that they originated. The information must be reported if the “spread” between the annual percentage rate (“APR”) on the loan and the yield on comparable Treasury instruments is at least 3 percentage points for first-lien loans or 5 percentage points for subordinate-lien loans. The spread between the APR and the Treasury rate, not the actual APR, is reported.
- HOEPA status (whether originated or purchased loans are covered by the Home Ownership and Equity Protection Act of 1994 [“HOEPA”]), which is determined by whether the upfront fees or annual percentage rate (“APR”) on the loan exceed specified thresholds.
- Lien status (loan is secured by a first or subordinate lien on a dwelling or is not secured by a dwelling). This field applies to originated loans and applications that do not result in an origination.
- **Collection of information.** Covered lenders must collect all the information that must be reported. Regulation C provides a form for collection of race, ethnicity, and sex information, which includes a notice explaining that providing the information is voluntary but, when the application is taken in person, the lender will determine race and ethnicity on the basis of visual observation and surname. In telephone applications, the disclosures must be made orally. As noted, collection and reporting of race, ethnicity, and sex is optional for purchased loans.

⁴ See 12 C.F.R. §§ 528.6 (OTS), 27.3(a) (OCC).

- **Disclosure of information.** HMDA requires lenders to disclose their information to both the government and the public:
 - The lender must submit information from its LAR to the FRB by March 1 of the year following the year the data were compiled.
 - The lender must provide a copy of a “modified LAR” to any member of the public on request, beginning on March 31 of each year for a request received on or before March 1, and within 30 days of the request thereafter. The LAR must be modified to remove identifying information (the application or loan number, the date that the application was received, and the date action was taken). At the lender’s option, the modified LAR may be provided in electronic form on request.
 - The Federal Financial Institutions Examination Council (“FFIEC”) uses each lender’s LAR to compile a disclosure statement for that institution, tabulating its lending data by various demographic parameters. This statement is generally available by September 1. Lenders must make the disclosure statement available to the public on request, and the FFIEC now posts all of the HMDA disclosure statements on its web site.
 - The FFIEC also produces aggregate reports of the HMDA data, including nationwide, metropolitan, and census-tract tabulations. These reports are also posted on the FFIEC web site.

Phase 1 of HMDA History: Depository Institution Community Reinvestment/Disinvestment Model

Background

When HMDA was enacted, most loans other than those guaranteed by the Federal Housing Administration (“FHA”) or another government agency were still being made by savings and loan associations or banks and funded by their deposit liabilities.⁵ Development of the secondary mortgage market, which was a precondition to the establishment of a nationwide residential mortgage industry, was still in its early stages. Community advocates and urban politicians argued that depository institutions were withdrawing their investments from, or “disinvesting” in, the communities from which they drew their deposits. This view was reflected in the House Report on the bill that created the beginnings of the HMDA reporting system:

The withdrawal of private investment capital for home mortgage loans and rehabilitation loans from an increasing number of geographic areas, principally within the nation’s major metropolitan centers, exacerbates the problem of providing public sector investments to stabilize and rehabilitate essentially older neighborhoods within our cities and adds to the frustration of millions of Americans denied access to credit at reasonable rates of

⁵ See Kenneth G. Lore & Cameron L. Cowan, *Mortgage-Backed Securities: Developments and Trends in the Secondary Mortgage Market*, ch. 1:2 (West Group 2003).

interest for the sale, improvement and rehabilitation of residential housing.

The process has led to the introduction of the word “red-lining” [*sic*] which increasingly has served to polarize elements of our society in a manner wherein the dialogue has become entirely destructive, rather than constructive. As polarization intensifies, neighborhood decline accelerates. The purpose of this title is, by providing facts, to bring to an end more than a decade of “red-lining” charges and countercharges.⁶

The Chairman of the House Subcommittee that originally reported the bill stated:

Entire viable neighborhoods of our major central cities, such as Chicago, . . . find their neighborhoods deteriorating to an alarming degree due to the failure of our financial institutions to provide access to credit for the sale and resale and rehabilitation of existing homes, while these same institutions continue to receive the vast majority of their deposits from the citizens [of] these neighborhoods who desire to continue to remain in the neighborhoods of their birth.⁷

Thus, the model that underlay the original enactment of HMDA was that depository institutions were draining deposits from urban neighborhoods but failing to “reinvest” those funds in the same urban areas. Shortly thereafter, this model became the basis for enactment of the CRA. The CRA continues to apply only to insured depository institutions, although they have the option of having their affiliates’ activities considered.⁸

While the CRA imposes affirmative obligations on insured depository institutions to serve their communities, HMDA’s focus has always been on disclosing information about lending patterns. According to the report accompanying the 1975 bill, there was a “compelling necessity” for legislation because the Federal Home Loan Bank Board (“FHLBB”), which then regulated the savings and loans that were the main source of mortgage financing, was unwilling to require such disclosure by regulation:

[Subcommittee on Financial Institutions Supervision, Regulation and Insurance Chairman Fernand J. St Germain:] All they want to know is what institutions have a commitment to the neighborhoods

⁶ H. Rep. No. 94-561, 94th Cong., 1st Sess., at 4 (1975), *reprinted in* 1975 U.S.C.C.A.N. 2303, 2306.

⁷ *Id.* at 11, *reprinted in* 1975 U.S.C.C.A.N. 2303, 2312, *quoting* Subcommittee on Financial Institutions Supervision, Regulation and Insurance, Hearings on H.R. 12421, 94th Cong., 2d Sess. (Mar. 5, 1974) (remarks of Rep. St Germain).

⁸ *See* 12 U.S.C. § 2902(2) (“regulated financial institution” defined by reference to definition of “insured depository institution” in Federal Deposit Insurance Act [“FDIA”]); *see, e.g.*, FRB Regulation BB, 12 C.F.R. §§ 228.22-228.24.

from whence they are getting their deposits. Are they making a fair reinvestment in these neighborhoods?

Now, doesn't the Board have the necessary authority to require this information?

[FHLBB Chairman Thomas R. Bomar]: Mr. Chairman, our attorneys tell me that we do have the authority to require it. We have not required it.⁹

Thus, the original goal of HMDA was simply to require banks and savings and loan associations to make data about their lending patterns available to the public.

HMDA Requirements as of Enactment in 1975

Although both the amount and types of data to be reported and the lenders subject to HMDA have expanded considerably since enactment in 1975, the basic structure of the law that was established at enactment has continued.

Initially, HMDA only applied to depository institutions with assets of more than \$10 million that were located, or had a branch located, in a metropolitan area. If covered, these institutions included loans of their majority-owned subsidiaries. A bank or thrift was required to compile summary statistics about its "mortgage loans" and make the data "available . . . to the public for inspection and copying at" its home office and at least one branch office in each metropolitan area in which the institution had a branch, under FRB regulations. A "mortgage loan" subject to HMDA was defined as a loan secured by residential property or a home-improvement loan, regardless of whether that loan was secured. The Board's implementing regulations, however, have restricted the definition of a "mortgage loan" to loans that are made for the purchase of a dwelling, home-improvement loans, or refinancings of those types of loans. Thus, loans to investors, including loans for multi-family properties, are HMDA-reportable, but second-lien loans that are not made as part of a purchase or refinancing are only reportable if they are for the purpose of home improvement.

Institutions were required to tabulate "the number and total dollar amount of mortgage loans" that they either originated or purchased in each metropolitan area, as well as originations or purchases where the property securing the loan was outside any metropolitan area. (The definition of a metropolitan area has changed as the federal government shifted from "standard metropolitan statistical areas" to the current multi-tiered system.¹⁰)

The data also had to be further tabulated by census tract, where data on census tracts were "readily available at a reasonable cost, as determined by the" FRB, or otherwise by zip code. Counties with a population of 30,000 or less did not have to be broken down further. The data also had to be tabulated by the number and dollar amount of:

⁹ H. Rep. No. 94-561, 94th Cong., 1st Sess., at 11(1975), *reprinted in* 1975 U.S.C.C.A.N. 2303, 2312.

¹⁰ *See supra* note 2.

- FHA, Veterans Administration (“VA”), and Rural Housing Service loans;¹¹
- Loans made to investors who did not, at origination, intend to reside in the property; and
- Home improvement loans.

This structure has continued to the present, although there have been significant modifications along the way. For example, HMDA has never required reporting of second-lien loans made outside the context of a purchase or refinancing unless their purpose is home improvement.¹² Loans for other purposes, such as debt-consolidation or education, need not be reported.

1980 Amendments: Centralized Reporting

The original legislation addressed the demands of community groups to be given access to each institution’s loan data, but did not provide any centralized source that would allow comparison of different institutions’ lending patterns. Amendments adopted in 1980 required the FFIEC to compile aggregate lending data for every institution with its home office or a branch in each metropolitan area, and to create a depository for that information in each area.¹³ The FFIEC continues to maintain those lists, usually at libraries or planning agencies, although the data are now available online as well.¹⁴

The 1980 amendments also made other changes designed to make the data more meaningful and facilitate comparison among institutions. The amendments:

- Eliminated the option of tabulating loans by zip code rather than census tract;¹⁵
- Required institutions to tabulate their data on a calendar-year basis rather than use some other fiscal year;¹⁶ and
- Required institutions to use a standard format in reporting their data.¹⁷

The FFIEC was required to compile and make public aggregate lending data showing the lending activity of institutions by census tract, as well as by groups of census tracts that are categorized by location, age of housing stock, income level, and racial characteristics.¹⁸ Those amendments

¹¹ See 12 U.S.C. § 2803(b)(1).

¹² See 12 U.S.C. § 2802(1).

¹³ See Pub. L. 96-399, § 340(c), 94 Stat. 1658, *adding* 12 U.S.C. 2809 (1980).

¹⁴ See <http://www.ffiec.gov/hmda/history2.htm>.

¹⁵ See Pub. L. 96-399, § 340(a)(2), 94 Stat. 1658, *adding* 12 U.S.C. 2803(a)(2)(A) (1980).

¹⁶ See Pub. L. 96-399, § 340(a)(3), 94 Stat. 1658, *adding* 12 U.S.C. 2803(d) (1980).

¹⁷ See Pub. L. 96-399, § 340(a)(3), 94 Stat. 1658, *adding* 12 U.S.C. 2803(e) (1980).

¹⁸ See Pub. L. 96-399, § 340(c), 94 Stat. 1658, *adding* 12 U.S.C. 2809 (1980).

also required HUD to compile aggregate lending data for FHA lending by institutions that were not subject to HMDA.¹⁹

By making the data available in a centralized location (albeit initially in a different location in each metropolitan area), requiring the FFIEC to do the work of correlating census tract numbers with demographic information about those areas, and, for the first time, requiring HUD to compile data about non-bank lenders, the 1980 amendments to HMDA took the first step in moving to a model of HMDA as a means of obtaining information about discrimination rather than simply about investment patterns of depository institutions. But because HMDA still provided no information about specific loans or the application process, the focus of HMDA remained on the extent to which institutions were lending in the communities in which their branches were located, and not on how any institution dealt with individual applicants.

1987 Amendments: Extending HMDA to Holding-Company Affiliates

During the 1980s, banks and thrifts increasingly moved their residential mortgage lending activities out of the institution itself and into a holding-company affiliate. In response, the 1987 amendments to HMDA (which became effective in 1988) applied the law for the first time to subsidiaries of bank and savings-and-loan holding companies.²⁰ This was another step away from strict consideration of depository institutions' lending activities in the areas where they took deposits, but the limited legislative history of the provision suggests that the rationale for the change was to get a better picture of the entire banking organization's lending activities and not to broaden the focus of the legislation to include mortgage lenders in general. As Senator Metzenbaum, one of the proponents of the change, explained it:

Mortgage banking affiliates of bank and S&L holding companies are becoming increasingly important players in providing mortgage finance, often conducting the bulk of mortgage lending for a holding company. Yet, since this type of institution is not covered under HMDA, it is difficult to document how well they serve older urban neighborhoods. Thirteen of the twenty-five largest mortgage companies are controlled by banks and their holding companies.²¹

Under the FRB regulations implementing the 1987 amendments, a "mortgage banking subsidiary" of a bank holding company or savings and loan holding company was subject to HMDA if at least 10% of its dollar loan volume consisted of "home purchase loans" (including refinancings of home purchase loans).²² As noted, majority-owned subsidiaries of banks and

¹⁹ See Pub. L. 96-399, § 340(c), 94 Stat. 1658, *adding* 12 U.S.C. 2810 (1980).

²⁰ See Housing and Community Development Act of 1987, Pub. L. 100-242, § 565, *amending* 12 U.S.C. § 2802(2) *and adding* 12 U.S.C. § 2803. Under 12 U.S.C. § 2803(g), mortgage-banking holding company subsidiaries were not required to report FHA loans.

²¹ 133 Cong. Rec. S4135-04, 1987 WL 934123 (Cong. Rec.) (Mar. 30, 1987).

²² See Board of Governors of the Federal Reserve System, Final Rule: Home Mortgage Disclosure, 53 Fed. Reg. 31683, 31688 (Aug. 19, 1988), *codified at* 12 C.F.R. § 203.2(e)(1)(ii) ("mortgage banking subsidiary" included in definition of "financial institution"), (g) (definition of "home purchase loan").

thrifts did not report separately; if the parent institution was subject to HMDA, the subsidiary's data were consolidated with those of the parent.²³ Mortgage banking subsidiaries, like banks and thrifts, were exempt from reporting if they had \$10 million or less in assets or had neither a home office nor a branch in a metropolitan area.²⁴

The 1987 amendments also made HMDA permanent.²⁵ Previously the law contained a sunset clause that required it to be periodically reauthorized.

Phase 2 of HMDA History: Mortgage Lender Discrimination Model

1989: FIRREA

The 1989 amendments to HMDA were a small part of the Financial Institutions Reform, Recovery, and Enforcement Act of 1989 ("FIRREA"), the legislation that extensively reformed and restructured the savings-and-loan industry.

The explicit goal of the 1989 changes was to allow HMDA to be used as a tool to detect discrimination. The section of the bill that made the changes was captioned "Fair Lending Oversight and Enforcement,"²⁶ and the Conference Report on the legislation stated:

The Home Mortgage Disclosure Act, as amended by this Act, requires among other things reporting by mortgage lenders to the appropriate regulatory agencies. A primary purpose of such reporting is to assist regulatory agencies in identifying possible discriminatory lending patterns that warrant closer scrutiny. To accomplish this purpose, it is essential that the data submitted to the agencies be in a form that facilitates the task of identifying any discriminatory lending patterns that disadvantage women, minority borrowers, or predominantly minority or low- or moderate-income neighborhoods.²⁷

The legislation made dramatic changes in both the range of institutions covered and the amount of information that lenders were required to report:

- Mortgage lenders that were not affiliated with banks, thrifts, or their holding companies were now subject to HMDA.²⁸

²³ 53 Fed. Reg. at 31688, *codified at* 12 C.F.R. § 203.2(e)(2).

²⁴ 53 Fed. Reg. at 31688, *codified at* 12 C.F.R. § 203.3(a).

²⁵ See Housing and Community Development Act of 1987, Pub. L. 100-242, § 565(b), *repealing* former 12 U.S.C. § 2811.

²⁶ FIRREA, Pub. L. 101-73, 103 Stat. 183, § 1211.

²⁷ H.R. Conf. Rep. No. 222 at 459, 1989 WL 168167 at *498 (Leg.Hist.), 101st Cong., 1st Sess. (1989).

²⁸ FIRREA, Pub. L. 101-73, 103 Stat. 183, § 1211(d), *adding* 12 U.S.C. § 2802(2)(B).

- Lenders would now have to report on “completed applications” as well as originations and purchases, including reporting withdrawn and rejected applications.²⁹ The lender could optionally also report the reasons for action taken.³⁰
- For most loans, the lender would have to determine and identify the race, sex, and income of loan applicants and borrowers.³¹ Loans purchased from another lender were exempt from this requirement, as were loans originated by depository institutions with assets of \$30 million or less.³²
- Lenders were also required to identify the “class” of purchaser of a loan.³³ As this requirement was implemented in FRB Regulation C, lenders were required to identify the agency purchasers, such as Fannie Mae, Freddie Mac, or Ginnie Mae, by name, and use a generic indication if the loan is sold to another type of institution such as a commercial bank or life insurance company.³⁴

The FRB’s implementing regulations modified the tests for HMDA coverage:

- Commenters had criticized the \$10-million-asset test because “mortgage companies’ assets tend to be low relative to the volume of loans that they originate.”³⁵ In response, although the regulations retained the exemption for independent lenders with \$10 million or less in assets, assets of the company’s parent were now included in the calculation.

²⁹ FIRREA, Pub. L. 101-73, 103 Stat. 183, § 1211(c), *amending* 12 U.S.C. § 2803(a)(1). A “completed application” was defined as “an application in which the creditor has received the information that is regularly obtained in evaluating applications for the amount and type of credit requested.” *See* FIRREA, Pub. L. 101-73, 103 Stat. 183, § 1211(e), *adding* 12 U.S.C. § 2802(3).

³⁰ FIRREA, Pub. L. 101-73, 103 Stat. 183, § 1211(b), *adding* 12 U.S.C. § 2303(h).

³¹ FIRREA, Pub. L. 101-73, 103 Stat. 183, § 1211(a), *adding* 12 U.S.C. § 2303(b)(4).

³² FIRREA, Pub. L. 101-73, 103 Stat. 183, § 1211(b) and (j), *adding* 12 U.S.C. § 2303(h), (i). Although the FIRREA amendments did not specifically state that loans purchased from another lender were exempt from reporting of demographic information, the Board apparently inferred that they were exempt based on this language in 12 U.S.C. § 2303(h):

These regulations shall also require the collection of data required to be disclosed under subsection (b)(4) with respect to loans sold by each institution reporting under this title, and, in addition, shall require disclosure of the class of the purchaser of such loans.

The FRB apparently interpreted the requirement to issue regulations requiring institutions to collect data for loans that they sell as implying that data need not be collected for loans that an institution purchases. *See* Board of Governors of the Federal Reserve System, Final Rule: Home Mortgage Disclosure (“Final FIRREA HMDA Rules”), 54 Fed. Reg. 51356, 51360 (Dec. 15, 1989) (“[t]he FIRREA requirement for reporting data on race or national origin, sex, and income does not apply to purchased loans”).

³³ FIRREA, Pub. L. 101-73, 103 Stat. 183, § 1211(b), *adding* 12 U.S.C. § 2303(h).

³⁴ *See* Final FIRREA HMDA Rules, 54 Fed. Reg. at 51366, *codified at* 12 C.F.R. part 203 app. A, § II.C.5 (1990 ed.).

³⁵ 54 Fed. Reg. at 51359.

- An unaffiliated mortgage lender was covered if it either had a home or branch office in a metropolitan area or “received applications for, originated, or purchased five or more home purchase or home improvement loans on property located in that” area.³⁶ Coverage of institutions with no branches in a metropolitan area represented another move away from the model of HMDA as measuring whether deposit-taking institutions “reinvest” in the communities where they take deposits.
- Mortgage banking subsidiaries of holding companies were now treated the same as unaffiliated lenders — they were subject to the same tests for coverage as those lenders, and their HMDA data were no longer consolidated with those of the parent company.³⁷
- The regulations retained the exemption for institutions with less than 10% of loan assets in home purchase and refinancing loans.³⁸

In implementing the statute, the FRB decided to take over responsibility for summarizing the data from lenders. Accordingly, the Board created a standard Loan/Application Register (“LAR”) form that contained a redacted entry for each completed application or originated or purchased loan. The information from the LAR was incorporated into a summary report for each institution by metropolitan areas, and the same information was used to issue aggregate reports.³⁹

Finally, FIRREA also brought United States branches of foreign banks under HMDA.⁴⁰

The Fed Studies

Lenders have long been required to collect racial, ethnic, and gender information about applicants under both Regulation B and specific banking regulations, but this information was not publicly disclosed until the expansion of HMDA reporting. In addition, the value of the information was limited because different requirements applied to different types of lenders.⁴¹

³⁶ 54 Fed. Reg. at 51363, *codified at* 12 C.F.R. § 203.2(c)(2).

³⁷ *See* 54 Fed. Reg. at 51359 and 51363, *codified at* 12 C.F.R. § 203.2(e)(2).

³⁸ *See* 54 Fed. Reg. at 51363, *codified at* 12 C.F.R. § 203.3(a)(2).

³⁹ *See* Board of Governors of the Federal Reserve System, Proposed Rule: Home Mortgage Disclosure, 54 Fed. Reg. 41255, 41258 (Oct. 6, 1989).

⁴⁰ *See* FIRREA, Pub. L. 101-73, 103 Stat. 183, § 1211(d), *amending* 12 U.S.C. § 2302(2). The definition of a “bank” was changed to incorporate by reference the definition of the term in the FDIA, 12 U.S.C. § 1813(a). At the same time, FIRREA amended the FDIA definition to include branches of foreign banks. *See* FIRREA, Pub. L. 101-73, 103 Stat. 183, § 204(a).

⁴¹ For example, lenders that were not subject to the jurisdiction of banking regulators were initially required under Regulation B to maintain monitoring information about purchases (but not refinancings) of 1-4-family residential real property. *See* Board of Governors of the Federal Reserve System, Amendments to Regulation B to Implement the 1976 Amendments to the Equal Credit Opportunity Act, 42 Fed. Reg. 1242, 1261-62 (Jan. 6, 1977), *adding* 12 C.F.R. § 202.13. In 1985, the requirement was expanded to include refinancings and to include the principal dwelling of the applicant even if it was not real property, but to exclude investor purchases (which are covered by HMDA). *See* Board of Governors of the Federal Reserve System, Revision of Regulation B, Final Rule and Final Official Staff Interpretation, 50 Fed. Reg. 48018, 48033 (Nov. 20, 1985). The Regulation B requirement has also never covered home-improvement loans. The banking regulators imposed their own, different requirements. *See, e.g.*, 12 C.F.R. §§ 27.3(b)(2) (OCC), 338.4(a)(1)(C) & (D) (Federal Deposit Insurance Corporation), & 528.6(d)(2)(v) (OTS) (1989 ed.). For example, the OCC required

Thus, the expansion of HMDA reporting made the magnitude of denial-disparity ratios clear for the first time.

Consumer advocates quickly responded to the public disclosure of the HMDA data by asserting that the disparity reflected discrimination.⁴² FRB staff members published two articles, one in 1991 just after the first year's expanded data had been collected, and another a year later, indicating that the black rejection rate in the database was more than twice the rate for white applicants.⁴³ Both FRB articles noted that many factors other than race, such as income and underwriting factors, also contribute to disparities in rejection rates.⁴⁴

Nevertheless, the release of the HMDA data, coupled with analyses based on the data, led many to believe that there was a serious problem of discrimination in mortgage lending. In response to the release of the HMDA data and concerns about differential denial rates, the Federal Reserve Bank of Boston attempted to overcome the limitations of the data by obtaining application data from 130 Boston-area banks that contained data used in underwriting. The Boston Fed Study compared denial rates of whites and minorities (African-Americans and Hispanics), taking into account factors such as credit history and loan-to-value ratio in addition to the factors reported in the HMDA data.⁴⁵ Although the study found that much of the disparity in reported HMDA results was attributable to these and other legitimate factors, the final version of the study concluded that minority applicants were about 80% more likely than whites to be denied a loan, even after considering underwriting factors that are not included in the HMDA data.⁴⁶

The Boston Fed Study was very controversial. Critics noted the many data errors in the data used to construct the model.⁴⁷ Observers who questioned the Boston Fed Study also argued that

the collection of information on purchases, construction-to-permanent loans, and refinancings, while the OTS required it for all loans related to a dwelling. Until recently, the Federal Housing Administration ("FHA") also maintained a program of "negative reporting," in which FHA lenders that were exempt from reporting under HMDA notified HUD annually that they were exempt. See FHA Mortgagee Letter 95-3: Home Mortgage Disclosure Act (HMDA) Update (January 5, 1995) (instituting the program); Memorandum from Patricia Dykes, Manager, CRA/HMDA Operations Unit, Federal Reserve Board (Nov. 23, 2004), available at <http://www.ffiec.gov/hmda/pdf/HUDtransfer.pdf> (announcing discontinuance of program).

⁴² See, e.g., Susan Schmidt, *Lending Bias Abounds, Says Housing Group*, Wash. Post, Dec. 20, 1991, at B10.

⁴³ See Glenn B. Canner & Dolores S. Smith, *Home Mortgage Disclosure Act: Expanded Data on Residential Lending*, 77 Fed. Reserve Bull. 859 (1991); Glenn B. Canner, *Expanded HMDA Data on Residential Lending: One Year Later*, 78 Fed. Reserve Bull. 859 (1992).

⁴⁴ See *id.*

⁴⁵ Alicia H. Munnell *et al.*, *Mortgage Lending in Boston: Interpreting HMDA Data*, Fed. Res. Bank of Boston, Working Paper WP-92-7 (Oct. 1992), presented in revised form in Alicia H. Munnell, *et al.*, *Mortgage Lending in Boston: Interpreting HMDA Data ("Boston Fed Study II")*, 86 Am. Econ. Rev. 25 (1996), vol. 86, no. 1 (Mar. 1996).

⁴⁶ *Boston Fed Study II* at 26 (noting a ratio of 1.8 to 1 in denial rates, which equates to an 80% increased likelihood of being denied for minorities).

⁴⁷ See Stanley D. Longhofer, *Discrimination in Mortgage Lending: What Have We Learned?*, in Fed. Res. Bank of Cleveland, 1996 Economic Commentary, available at <http://www.clevelandfed.org/Research/com96/081596.htm> (last visited Feb. 21, 2005), citing David K. Horne, *Evaluating the Role of Race in Mortgage Lending*, 7 FDIC Banking Rev. 1-15 (1994); Ted Day & Stan J. Leibowitz, *Mortgages, Minorities, and Discrimination*, University of Texas at Dallas, unpublished manuscript (1993).

the design of the study was flawed for other reasons. These issues raised by the Boston Fed Study are discussed in more detail below, along with an analysis of the severe limitations of HMDA data as evidence of discrimination.

In any case, the premise of the Boston Fed Study was that HMDA data, standing alone, were insufficient to demonstrate or disprove that a lender was discriminating. Therefore, it was necessary to augment the HMDA information with additional information that the lender considered in underwriting. As also discussed below, despite the continuing controversy over the validity of the Boston Fed Study, government agencies charged with enforcing the fair lending laws do not regard HMDA data by themselves as evidence of discrimination. They also have declined to use statistical analysis of HMDA data that has been “augmented” with additional information about the underwriting process that is not reported under HMDA as a tool to detect discrimination.

Industry Response to the 1989 HMDA Data and Studies

Although lenders shared the skepticism of many scholars as to whether the Boston Fed Study demonstrated discrimination or simply reflected disparities in the economic position of whites and minorities, the industry responded proactively to criticisms of their minority and low-income lending records. Mortgage lenders:

- Instituted programs such as “second review” procedures, in which some or all rejected minority applications were reviewed to ensure that the consumer had been treated fairly and that all potential products had been considered.⁴⁸
- Expanded their underwriting standards to eliminate unnecessary impediments to loan approvals, and created new products that were more accessible to low-income and credit-impaired borrowers.
- Worked with the GSEs to make the GSEs’ underwriting standards more flexible and more suitable for those borrowers and to develop new products aimed at that market.
- Expanded outreach programs.

The changes in lenders’ practices had a significant impact on the availability of credit to lower-income and minority borrowers. For example, “[a]nnual mortgage originations for African-Americans, Hispanics, and members of other minority groups . . . jumped about 130%” between 1990, the first year of expanded HMDA reporting, and 1996 — a rate that was “nearly twice the growth rate of the total market.”⁴⁹

⁴⁸ See, e.g., Barbara Rehm, *New Action on Minority Loan Front: Mortgage Group Prepares to Sign Pact with HUD*, Am. Banker, Aug. 23, 1994, at 1 (describing agreement between trade association and Department of Housing and Urban Development that specified fair-lending best practices, including a second review program).

⁴⁹ Jaret Seiberg, *Banks Making Good Progress In Their Fair-Lending Efforts*, Am. Banker, Sept. 16, 1996, at 1.

1991: Change in Small Mortgage-Banker Exemption

Although the FRB had modified the \$10 million asset cutoff to include assets of the parent corporation, critics continued to contend that the exemption was inappropriate for non-bank mortgage banking companies because they generally do not hold assets in portfolio, and, therefore, have low assets compared to a depository institution with a similar level of lending activity. Congress in 1991 replaced the fixed amount with a directive to the Board to set a cutoff for mortgage bankers that is comparable to the figure for banks and thrifts.⁵⁰

In implementing the congressional directive, the FRB expanded the definition to include some non-bank lenders with assets under \$10 million. It adopted a three-part test for coverage of “a for-profit mortgage-lending institution (other than a bank, savings association, or credit union).” Such a lender was covered if it:

- Originated home-purchase loans in the preceding calendar year (including refinancing of purchase loans) equal to 10% of its loan-origination volume;
- Had a home or branch office in a metropolitan area as of the preceding December 31; and
- Either had assets of more than \$10 million, including the assets of any parent, as of the preceding December 31, or originated at least 100 home-purchase loans, including refinancings of such loans, in the previous calendar year.⁵¹

1992: LARs Must Be Disclosed

As noted, the disparity in rejection rates reported in the FRB articles generated very negative publicity for the mortgage industry, particularly because much of the reporting did not include the caveat in those articles recognizing that comparative rejection rates are not, in themselves, evidence of discrimination. The Housing and Community Development Act of 1992 reflected the attention that the new HMDA data had generated — it required institutions to disclose the contents of their LAR to the public, with information that would compromise privacy deleted.⁵² Institutions must provide the modified LAR by March 31 of each year, for a request received by March 1, and within thirty days of a request received after March 31.⁵³ They may charge a reasonable fee for the disclosure.⁵⁴

The 1992 amendments also set deadlines for the FFIEC to produce its reports — September 1 for the reports of each institution’s activity and December 1 for the aggregate reports. The FFIEC

⁵⁰ See Federal Deposit Insurance Corporation Improvement Act of 1991, Pub. L. 102-242, 105 Stat. 2236, § 224, *amending* 12 U.S.C. § 2808(a).

⁵¹ See Board of Governors of the Federal Reserve System, Final Regulatory Amendments: Home Mortgage Disclosure, 57 Fed. Reg. 56963, *codified at* 12 C.F.R. § 203.3(a)(2)(ii) (Dec. 2, 1992).

⁵² Housing and Community Development Act of 1992, Pub. L. 102-550, § 932(a), 106 Stat. 3672, *adding* 12 U.S.C. § 2803(j).

⁵³ *Id.*

⁵⁴ Housing and Community Development Act of 1992, Pub. L. 102-550, § 932(a), 106 Stat. 3672, *adding* 12 U.S.C. § 2803(j).

was also strongly encouraged, as of 1994 and succeeding years, to begin producing the institution-specific reports by July 1 and the aggregate reports by September 1.⁵⁵

Thus, the FRB's decision to require submission of LARs — framed as a way of easing lenders' compliance burden — resulted in short order in some significant details about each loan being made available to the public, with the potential for fair lending liability.⁵⁶ Although the direct burden of providing the LARs may be lower than the old system that required lenders to assemble the information, the cost of a fair lending lawsuit or government enforcement action generated by the data in the LARs could far exceed any savings from having the FFIEC perform the analysis.

1996: Updated and Indexed Small-Bank Exemption

In 1996, the small-depository-institution exemption was indexed for the cost of living. A one-time adjustment was made from \$10 million to \$28 million for the increase in the Consumer Price Index from 1975 to 1996, and the law provided for annual indexing thereafter.⁵⁷ The level for 2005 is \$34 million.⁵⁸ The exemption for non-banking lenders, however, was still based on the equivalent of a \$10-million-asset depository institution.⁵⁹

The 1996 amendments also made other changes designed to “reduce [the] compliance burden” created by HMDA:

- A lender could avoid having to maintain copies of LARs and disclosure statements at a branch in each metropolitan area by posting a notice in at least one branch per area that the information was available at its home office on request. The home office was required to provide the information relating to the location of a branch within 15 days of receiving a request.⁶⁰
- Lenders were also given the option of providing the information using an electronic medium such as a computer disk, if this format was acceptable to the requester.⁶¹

⁵⁵ Housing and Community Development Act of 1992, Pub. L. 102-550, § 932(a), 106 Stat. 3672, *adding* 12 U.S.C. § 2803(l).

⁵⁶ *See, e.g.,* Allen J. Fishbein, *Fair Housing Conference: Home Mortgage Disclosure Act Report*, 28 J. Marshall L. Rev. 343 (1995).

⁵⁷ *See* Economic Growth and Regulatory Paperwork Reduction Act of 1996 (“EGRPRA”), Pub. L. 104-208, § 2225(a), 110 Stat. 3009, *adding* 12 U.S.C. § 2808(b). The Board made the initial adjustment by regulation. *See* Board of Governors of the Federal Reserve System, Home Mortgage Disclosure: Interim Rule, 62 Fed. Reg. 3603 (Jan. 24, 1997); Board of Governors of the Federal Reserve System, Home Mortgage Disclosure: Final Rule, 62 Fed. Reg. 28620 (May 27, 1997).

⁵⁸ *See* Board of Governors of the Federal Reserve System, Home Mortgage Disclosure: Final Rule and Staff Commentary, 69 Fed. Reg. 77139 (Dec. 27, 2004).

⁵⁹ *See* EGRPRA, Pub. L. 104-208, § 2225(a), 110 Stat. 3009, *adding* 12 U.S.C. § 2808(b).

⁶⁰ *See* EGRPRA, Pub. L. 104-208, § 2225(b), 110 Stat. 3009, *adding* 12 U.S.C. § 2803(m)(1).

⁶¹ *See* EGRPRA, Pub. L. 104-208, § 2225(b), 110 Stat. 3009, *adding* 12 U.S.C. § 2803(m)(2).

Phase 3 of HMDA History: Predatory Lending/Pricing Discrimination Model

The changes in lender policy in response to the expansion of HMDA reporting were one contributing factor in the growth of lending to a wider range of borrowers. Another factor was the development of credit scoring technology, which facilitated the creation of a secondary market for nontraditional loans. As a result of these developments, more and more consumers were able to obtain loans, but there was much greater variation in pricing. In addition, the “predatory lending” issue drew increasing attention from advocates and some members of Congress. Lenders were now being criticized, not for redlining — avoiding minority and low-income areas — but for “targeting” or “reverse redlining” — expressly seeking out minority or low- and moderate-income borrowers for nonprime loans at higher rates and more onerous terms than conventional conforming loans.

The third phase of HMDA reflects the change in focus to predatory lending and the nonprime market. In addition, the FRB has attempted to improve the general quality and consistency of HMDA reporting and of how it is presented. In contrast to the first two phases, the recent extensive changes to HMDA requirements have been driven entirely by regulation. There has been no new legislation requiring additional reporting.

The most recent revisions grew out of the FRB’s periodic review of Regulation C (as well as its other regulations).⁶² The most significant change was to require lenders, as of January 1, 2004, to report loan pricing on loan originations with rates above a certain threshold — those in which the APR exceeds the yield for comparable Treasury securities by 3 percentage points for first-lien loans and 5 percentage points for subordinate-lien loans.⁶³ The spread over comparable Treasuries, rather than the actual APR, is reported.⁶⁴ Along the same lines, lenders must report the lien status of the loan, whether it is covered by HOEPA, and whether it is secured by a manufactured home.⁶⁵ The FRB hopes that this information will reveal more information about whether certain lenders are targeting minorities or lower-income borrowers for above-threshold loans:

Obtaining loan pricing data is critical to address fair lending concerns related to loan pricing and to better understand the mortgage market, including the subprime market. The mortgage marketplace has changed significantly since HMDA was enacted and continues to evolve. Along with a substantial growth in the subprime market has come increased variation in loan pricing, generally related to an assessment of credit risk. In light of these changes, the Board believes that the collection of loan pricing

⁶² See Board of Governors of the Federal Reserve System, Home Mortgage Disclosure: Advance Notice of Proposed Rulemaking, 63 Fed. Reg. 12329 (Mar. 12, 1998).

⁶³ See Board of Governors of the Federal Reserve System, Home Mortgage Disclosure: Final Rule and Staff Interpretation, 67 Fed. Reg. 43218, 43223 (June 27, 2002), *amending* 12 C.F.R. § 203.4(a).

⁶⁴ *See id.*

⁶⁵ *See id.*; see Board of Governors of the Federal Reserve System, Home Mortgage Disclosure: Final Rule and Staff Interpretation, 67 Fed. Reg. 7222, 7223, and 7237 (Feb. 15, 2002), *amending* 12 C.F.R. § 203.4(a).

information is necessary to fulfill the statutory purposes of HMDA and to ensure the continued utility of the HMDA data.⁶⁶

The FRB also adopted several changes designed to improve the quality and precision of HMDA data. Most significantly, as noted above, HMDA had long required lenders to collect race, ethnicity, and gender information about applicants, including making a judgment about those factors if the applicant declined to state it in a face-to-face interview. But lenders were not required to request the information in a telephone application. Because of the increasing number of applications taken by telephone, the regulation was amended as of January 1, 2003, to require lenders to request the information in those applications.⁶⁷

The FRB made other, technical changes designed to improve the consistency of HMDA reporting, which went into effect on January 1, 2004. They included:

- The definitions of refinancings and home-improvement loans were made more precise, and lenders lost the option of treating certain loans as refinancings when they did not meet the precise definition.⁶⁸
- HMDA now applies to certain applications for “preapproval,” defined narrowly to cover only loans that are fully underwritten and in which the lender issues a written, time-limited commitment in which the only substantive condition is locating a suitable property.⁶⁹

Finally, the FRB expanded coverage of nondepository lenders by including lenders that make \$25 million or more in mortgage loans under HMDA even if less than 10% of their loan-origination volume was home-purchase loans or refinancings of those loans.⁷⁰ Previously, many nonprime lenders that focus on providing home equity loans had not been HMDA reporters because of this exemption.

II. Limitations of the HMDA Data and of Statistical Analysis of Discrimination

The HMDA Data Are Not Evidence of Discrimination

The federal agencies that enforce the fair lending laws generally do not use HMDA data directly in enforcing these laws, because the HMDA data do not include the factors actually considered

⁶⁶ Board of Governors of the Federal Reserve System, Home Mortgage Disclosure: Final Rule and Staff Interpretation, 67 Fed. Reg. at 7228 (Feb. 15, 2002).

⁶⁷ See Board of Governors of the Federal Reserve System, Home Mortgage Disclosure: Final Rule and Staff Interpretation, 67 Fed. Reg. 43217 (June 27, 2002), *amending* 12 C.F.R. part 203 app. A, § V.D.2.

⁶⁸ See Board of Governors of the Federal Reserve System, Home Mortgage Disclosure: Final Rule and Staff Interpretation, 67 Fed. Reg. 7222, 7223, & 7237, *amending* 12 C.F.R. § 203.2(g) and (k).

⁶⁹ See Board of Governors of the Federal Reserve System, Home Mortgage Disclosure: Final Rule and Staff Interpretation, 67 Fed. Reg. 7222, 7223, *adding* 12 C.F.R. § 203.2(b)(2).

⁷⁰ See Board of Governors of the Federal Reserve System, Home Mortgage Disclosure: Final Rule and Staff Interpretation, 67 Fed. Reg. 7222, 7223, *adding* 12 C.F.R. § 203.2(e)(2)(i)(B). Institutions with \$25 million in mortgage-loan volume still had to (1) have a home or branch office in a metropolitan area; and (2) either have assets, including assets of a parent, of more than \$10 million; or have made at least 100 home-purchase loans (including refinancings of such loans) in the previous year. 12 C.F.R. § 203.2(e)(2)(ii) and (iii).

in determining whether a loan is to be made and at what price. Most significantly, the data do not indicate the underwriting factors that are most important to the loan decision, including the lender's assessment of the applicant's credit and employment history, the applicant's assets, and debt-to-income and loan-to-value ratios.

Because of these limitations, the banking agencies, which have created specific enforcement procedures, use the data as an "indicator" of potential redlining. More significantly, since the main method of enforcement is to compare minority and non-minority "marginal applicants," the agencies use HMDA data to identify those applicants.⁷¹ They do not attempt to replicate the approach of the Boston Fed Study of augmenting the HMDA data with other information to construct a statistical model of lending performance.

The FRB and other government agencies charged with collecting the data and enforcing the law have recognized that HMDA data cannot prove illegal discrimination. One of the FRB staff articles on HMDA noted:

The HMDA data have clear limitations. Foremost among them is the general lack of information about factors important in assessing the creditworthiness of applicants and the adequacy of collateral offered as security on loans. Without such information, determining whether individual applicants have been treated fairly is not possible.⁷²

An Interagency Policy Statement on fair lending issued shortly after, and partially in response to, the Boston Fed Study made a similar point:

Data reported by lenders under the HMDA do not, standing alone, provide sufficient information for such an analysis because they omit important variables, such as credit histories and debt ratios. HMDA data are useful, though, for identifying lenders whose practices may warrant investigation for compliance with fair lending laws. HMDA data may also be relevant, in conjunction with other evidence, to the determination whether a lender has discriminated.⁷³

Reflecting these limitations, the FFIEC's fair lending examination procedures specifically instruct examiners *not* to treat patterns revealed by HMDA data as evidence of "disparate impact" discrimination:

Gross HMDA denial or approval rate disparities are not appropriate for disproportionate adverse impact⁷⁴ analysis because

⁷¹ The Justice Department also often follows the approach of comparing matched pairs of marginal applicants.

⁷² Glenn B. Canner, *supra note* 43.

⁷³ Department of Housing and Urban Development *et al.*, *Policy Statement on Discrimination in Lending*, 59 Fed. Reg. 18266, 18269 (Apr. 15, 1994).

⁷⁴ As described by the agencies, there are three main types of lending discrimination:

they typically cannot be attributed to a specific policy or criterion.⁷⁵

The FFIEC’s guidelines do permit consideration of patterns in HMDA data in identifying “indicators of potential discriminatory [r]edlining”⁷⁶ (a form of “disparate treatment” discrimination) where the HMDA data reveal “[s]ignificant differences in the number of loans originated in those areas in the lender’s market that have relatively high concentrations of minority group residents compared with areas with relatively low concentrations of minority residents.”⁷⁷ But the HMDA data are used only as an initial screen, not to prove that redlining is occurring.⁷⁸

Given the finding of the Boston Fed study that fair lending problems occurred with marginal applicants, rather than either highly qualified or clearly unqualified borrowers, the main use of HMDA data in banking agency fair lending enforcement is to help the examiner find “marginal” transactions for comparison.⁷⁹ The rationale for this approach is as follows:

A principal goal is to identify cases where similarly qualified prohibited basis and control group applicants had different credit outcomes, because the agencies have found that discrimination, including differences in granting assistance during the approval process, is more likely to occur with respect to applicants who are *not* either clearly qualified or unqualified, i.e., “**marginal**” applicants. The examiner-in-charge should, during the following steps, **judgmentally select** from the initial sample only those denied and approved applications which constitute **marginal transactions**.⁸⁰

Thus, the enforcement agencies have not attempted to use HMDA data or other statistics in the way that the Boston Fed did, in an attempt to demonstrate discrimination directly. Rather, the

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- [O]vert evidence of discrimination,” when a lender blatantly discriminates on a prohibited basis;
 - [E]vidence of “disparate treatment,” when a lender treats applicants differently based on one of the prohibited factors; and
 - [E]vidence of “disparate impact,” when a lender applies a practice uniformly to all applicants but the practice has a discriminatory effect on a prohibited basis and is not justified by business necessity.

Id., 59 Fed. Reg. at 18268 (Apr. 15, 1994).

⁷⁵ FFIEC, Interagency Fair Lending Examination Procedures, app. at 26 (1999), available at <http://www.ffiec.gov/pdf/fairappx.pdf> (emphasis in original).

⁷⁶ FFIEC, Interagency Fair Lending Examination Procedures at 8-9 (1999), available at <http://www.ffiec.gov/PDF/fairlend.pdf>.

⁷⁷ *Id.* at 9.

⁷⁸ *See id.* at 30.

⁷⁹ *See id.* at 16.

⁸⁰ *Id.* at 17 (emphasis in original).

HMDA data are generally used as an “indicator” that further “judgmental,” rather than statistical, inquiry is warranted, although they could also be used as part of a redlining case.

Although the banking agencies have not yet revised their examination procedures in light of the expanded HMDA data on pricing, in issuing the revised HMDA regulations, the Federal Reserve Board made it clear that it views the new information as a trigger for further inquiry, not as evidence, in itself, of discrimination:

This [pricing] information would facilitate identification of subprime loans, which have different characteristics, such as higher denial rates, from other mortgage loans. Pricing information could also help identify practices that raise *potential* fair lending concerns warranting further investigation.⁸¹

Weaknesses in the Boston Fed Study

Although the federal enforcement agencies recognize that HMDA data standing alone are insufficient to prove discrimination, it might be thought that they would support use of the approach taken in the Boston Fed Study, in which those data were supplemented with underwriting information. The Interagency Policy Statement appeared relatively soon after the initial Boston Fed Study was released and cites it favorably. For that reason, it is noteworthy that neither the Policy Statement nor the later FFIEC examiner guidelines endorses the use of augmented HMDA data to determine whether discrimination has occurred.

The agencies may have decided not to embrace the approach of the Boston Fed Study because of the many problems noted by critics in the design of that study. These issues included:

- The method of statistical analysis used, the “logit” method, can theoretically detect discrimination “where none exists, yet fail to uncover even egregious cases of bias.”⁸²
- Even with the augmented data in addition to HMDA information, the Boston Fed Study did not consider several factors that may have contributed to loan decisions, such as whether the borrower submitted information that could not be verified and whether the borrower met the institution’s guidelines.⁸³ Since those factors also correlate with race or ethnicity, part or all

⁸¹ Board of Governors of the Federal Reserve System, Home Mortgage Disclosure: Final Rule and Staff Interpretation, 67 Fed. Reg. 7222, 7229 (Feb. 15, 2002) (emphasis added).

⁸² Stanley D. Longhofer, *supra* note 47, citing Paul W. Bauer & Brian A. Cromwell, *A Monte Carlo Examination of Bias Tests in Mortgage Lending*, Fed. Res. Bank of Cleveland Econ. Rev., vol. 30, no. 3 at 27 (1994); Anthony M.J. Yezer, Robert F. Phillips, & Robert P. Trost, Bias in Estimates of Discrimination and Default in Mortgage Lending: The Effects of Simultaneity and Self-Selection,” *Journal of Real Estate Finance and Economics*, vol. 9, no. 3 (November 1994), pp. 196–215.

⁸³ See, e.g., Mark Zandi, *Boston Fed’s Bias Study Was Deeply Flawed*, *Am. Banker*, Aug. 19, 1993, at 13 (also noting that a housing recession that occurred during the period studied had a disproportionate impact on housing prices at the low end of the market, where minority borrowers are more likely to be found). See generally Stephen L. Ross & John Yinger, *The Color of Credit: Mortgage Discrimination, Research Methodology, and Fair-Lending Enforcement* 108-130 (2002).

of the difference in acceptance rates could be due to these legitimate omitted variables rather than to race or ethnicity.⁸⁴

- The model assumed that all lenders applied the same underwriting standards to each applicant. If this assumption is incorrect, then some of the differences in denial rates could reflect differences in the proportion of minorities and whites who apply to different institutions or who apply for specialized programs at different institutions. For example, if an institution operates an aggressive outreach program to attract more minority applicants (including those with marginal credit qualifications), it may, paradoxically, increase the ratio of minority to non-minority denials.⁸⁵
- If the assumption is that lenders were biased against minorities, minorities should have had, but did not have, lower default rates because they would have had to be better qualified to overcome the lender's biases. Advocates of this position included Nobel prizewinner Gary Becker.⁸⁶

Other analysts defended the Boston Fed Study, noting, for example, that Prof. Becker's analysis assumed that lenders had a "taste for discrimination" — *i.e.*, were willing to forgo profits in order to discriminate against minorities — while the law also prohibits "statistical" discrimination, in which the lender can profit by discriminating "if the overall pool of minority applicants is less creditworthy on average than the white applicant pool."⁸⁷

The enforcement agencies have apparently concluded, however, that the many unresolved questions in the Boston Fed Study outweigh whatever value that approach might have in drawing firm conclusions about discrimination in mortgage lending. As an economist with the Federal Reserve Bank of Cleveland put it:

So, does widespread discrimination exist in the home mortgage market? Ultimately, the answer must be "we don't know." Taken together, the problems with the Boston Fed data set (including its limited geographic focus), questions about the robustness of logit analysis, and limitations of other methods for detecting discrimination all combine to lead most economists to conclude that we still don't have a definitive answer about the presence of widespread and systematic discrimination in the home mortgage market.⁸⁸

⁸⁴ But see Jason Dietrich, *Under-Specified Models and Detection of Discrimination in Mortgage Lending*: OCC Economic and Policy Analysis Working Paper, March 2003, available at <http://www.occ.treas.gov/ftp/workpaper/wp2003-2.pdf> (no clear direction of increased or decreased discrimination when omitted variables were added in national bank fair lending examinations).

⁸⁵ See generally Stephen L. Ross & John Yinger, *supra* note 83, at 169-212 (2002).

⁸⁶ Gary S. Becker, *The Evidence Against Banks Doesn't Prove Bias*, Bus. Week, Apr. 19, 1993, at 18.

⁸⁷ Stanley D. Longhofer & Stephen R. Peters, *Beneath the Rhetoric: Clarifying the Debate on Mortgage Lending Discrimination*, Fed. Res. Bank of Cleveland Econ. Rev., 1998 quarter 4, at 5.

⁸⁸ Stanley D. Longhofer, *Discrimination in Mortgage Lending: What Have We Learned?*, *supra* note 47.

Even with Pricing Information, HMDA Data Will Not Show Discrimination

With the new reporting of pricing information, there will likely be claims that disparities in the incidence of higher-cost loans to minority groups are evidence of discrimination. As noted above, however, without information about the underwriting factors that lenders actually used, even the expanded HMDA data will not, in themselves, demonstrate that discrimination has occurred. Many components go into a pricing decision, including not only underwriting factors, which are not reported under HMDA, but also the dynamics of the market, which are influenced by both a lender's funding reserves at any given time and the borrower's specific choices as to loan terms. In addition, the APR spread is an imperfect measure of the cost of the loan to the consumer. For example, the APR does not reflect many closing costs and thus does not take into account a borrower's decision to avoid closing costs by paying a higher rate.

All of the complexities of modeling lending behavior that were identified as shortcomings of the Boston Fed Study negate any simplistic conclusions that might be drawn from HMDA price disparities. It is extremely difficult to capture all the factors that may have contributed to pricing decisions, especially when those factors include choices made by individual borrowers as to loan products, terms, loan amounts, and financing structures.

Conclusion

The focus of HMDA has gradually shifted from a concern with whether banks and thrifts were lending in the neighborhoods in which they collected deposits, to a more general inquiry into whether lenders of all types were discriminating, to the current emphasis on whether vulnerable groups, including minorities, are being targeted with unfavorable rates and terms. This shift has generally reflected changes in how mortgages are made, from an activity of local banks and savings and loans to a nationwide industry in which many of the major players are not depository institutions, although many are bank and thrift affiliates. Although the trend has been to collect more and more information, including pricing information, HMDA data still do not include most factors considered in underwriting, and, therefore, should not be used to conclude that a lender is discriminating. Moreover, because of the many problems in designing a valid study, even adding underwriting factors that the lender considered may not allow a firm conclusion as to whether it is engaged in discrimination.