

From Confrontation to Collaboration? Banks, Community Groups, and the Implementation of Community Reinvestment Agreements

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Abstract

Banks and other depository institutions have signed more than 300 community reinvestment agreements valued at \$350 billion in the two decades since the passage of the Community Reinvestment Act (CRA). This article examines the effectiveness of negotiating CRA agreements in Chicago, Cleveland, Pittsburgh, and New Jersey. After describing the agreements and the procedures by which they are enforced, the article looks at their impact and discusses several factors that could limit implementation of CRA agreements in the future.

The findings suggest that CRA agreements are more effective in some areas than others. They seem most consistently successful in meeting their goals for mortgages, investments in low-income housing tax credits, grant giving to community-based organizations, and in opening (and keeping open) inner-city bank branches. The future of CRA agreements is clouded by several factors, most notably the restructuring and consolidation of the financial service sector.

Keywords: Nonprofit sector; Underserved; Credit; Banks; Community Reinvestment Act

Introduction

Banks and other depository financial institutions have committed billions of dollars in mortgages and other loans and grants to low-income and minority households and neighborhoods. These financial commitments represent one result of the federal Community Reinvestment Act (CRA) of 1977. CRA requires banks and other lenders to serve all areas from which they draw deposits. Current CRA regulations require federal regulators to take into account lending, investments, and other services for low-income and minority residents when considering a bank's application for mergers, acquisitions, and other regulated actions. Equally important, CRA also allows community groups and other organizations to challenge a proposed merger or acquisition because of a bank's inadequate service to minorities or low-income households.

Armed with this legislation, community advocates across the United States have challenged proposed bank mergers and acqui-

tions, claiming that the banks failed to provide adequate service to low-income and minority families and neighborhoods. In response to these challenges, several hundred banks have negotiated community reinvestment agreements, pledging to improve mortgage lending and other services. Additionally, an increasing number of banks, including some of the nation's largest financial institutions, have launched voluntary community reinvestment commitments. For instance, in May 1998, shortly after announcing their intention to merge, Citicorp and Travelers Group unveiled a 10-year, \$115 billion plan to lend and invest in low- and moderate-income communities (O'Brien 1998). Around the same time, NationsBank and BankAmerica presented a 10-year, \$350 billion community reinvestment program soon after announcing their merger plans (O'Brien 1998). By 1997 more than 300 negotiated and voluntary agreements had been launched, amounting to more than \$353 billion (National Community Reinvestment Coalition [NCRC] 1998).

Until now, there has been little if any research on the outcomes of CRA agreements. Little is known about the extent to which banks have met the financial and other goals of their agreements, whether voluntary or negotiated. Most research has concentrated on mortgage lending, analyzing the incidence and extent of racial bias (see, for example, Goering and Wienk 1996; Munnell et. al 1992). To a lesser extent, some studies document the genesis of particular CRA agreements (Squires 1992). This article marks a new direction in CRA research by examining the outcomes of CRA agreements. Drawing on case studies of community reinvestment agreements in Chicago, Cleveland, New Jersey, and Pittsburgh, it explores how local governments and community groups monitor and enforce their agreements and assesses the outcomes of different aspects of the agreements. Before presenting the case studies, the article briefly discusses the evolution of CRA agreements and summarizes the results of a recent quantitative comparison of the mortgage lending of banks with and without CRA agreements. The case study discussion begins with an overview of the agreements in the four sites and the procedures by which they are monitored and enforced. The article then looks at the impacts of the agreements and considers several conditions that contribute to their success and factors that could limit the implementation of agreements in the future. It concludes with a discussion of policy implications and issues for additional research.

Most community groups did not begin to exercise their authority under CRA to challenge bank mergers and acquisitions until several years after the law's enactment in 1977. Only 16 CRA agreements were signed through 1983 (Christiano 1995, 107). But at least 147 agreements were initiated from 1984 through 1989 and more than 165 others were announced from 1990 through early

1996 (NCRC 1996). The proliferation of CRA agreements since the mid-1980s stems from several developments. One is the deregulation and rapid restructuring and consolidation of the financial services sector, including the bank and thrift industries. Because CRA enables community groups and other organizations to challenge bank mergers and acquisitions as well as applications to expand interstate banking, the industry's restructuring has given community groups numerous opportunities to negotiate CRA agreements. For example, the number of savings and loans declined by 52 percent and commercial banks by 30 percent from 1980 to 1995 (Avery et al. 1997), although not all of these institutions participated in mergers; many went out of business. A second factor is the reluctance the four federal financial regulatory agencies¹ have shown in the past to consider a bank's CRA performance in deciding to approve a proposed merger, acquisition, or other regulated activity. In 1988 the federal bank regulators testified in hearings before the Senate Banking Committee that in the previous 10 years they had denied only 8 of 40,000 bank applications because of inadequate compliance with CRA (Bradford and Cincotta 1992, 255; Christiano 1995, 110). The regulators' apparent reluctance to enforce CRA prompted community advocates to press their own CRA challenges.

CRA agreements express a bank's goals or commitments toward improving its services to minority and low-income households and/or neighborhoods. Agreements almost always include provisions for home mortgage lending. Some agreements present a variety of mortgage products in considerable detail, specifying the interest rate, the maximum mortgage origination fee ("points"), minimum down payment requirements, the need for private mortgage insurance (PMI), and borrower eligibility standards (income, debt-service-to-income ratios). Additionally, agreements increasingly encompass other areas, such as small business loans, home improvement loans, construction loans, permanent mortgages and other types of financing for new housing development, investments in low-income housing financed with low-income housing tax credits (LIHTCs), and grants and loans to community-based organizations. Some agreements pledge not to close bank branches, and some set goals for increasing the hiring of minority employees and purchasing more goods and services from minority-owned firms (see table 1 for an overview of CRA provisions and NCRC [1997] for more detailed examples of specific agreements).

In a previous article (Schwartz 1998), I compared the mortgage and home improvement lending of banks and thrifts with and without

¹ The four federal agencies that supervise bank CRA performance are the Federal Reserve Bank, the Office of the Comptroller of the Currency, the Federal Deposit Insurance Corporation, and the Office of Thrift Supervision (before 1989, the Home Loan Bank Board).

Table 1. Overview of CRA Agreements and Provisions: Subject Categories and Subcategories

Housing

- Specific Loan Targets
 - Single-family households
 - Nonprofit and minority housing developers
 - Multifamily households
 - Housing cooperatives, land trusts, and mobile homes/manufactured housing
- Loan Terms and Conditions
 - Low-interest loans
 - Waive or reduce closing costs
 - Waive or reduce points
 - Loan size
 - Down payments and private mortgage insurance
- Underwriting Standards
 - Credit history
 - Income source
 - Employment
 - Obligation ratios
- Participation in Public Programs/Loan Pools and Consortia
 - Federal Housing Administration and Veterans Administration programs
 - Federal Home Loan Bank programs
 - Low-income housing tax credits
 - Housing Finance Agency bonds
 - Public/private loan pools and consortia
- Other Forms of Housing Support
 - Loan counseling
 - Lending discrimination testing
 - Loan review
 - Foreclosed properties

Business and Economic Development

- Specific Loan Targets
 - Small business
 - Microbusiness
 - Minority- and women-owned businesses
 - Economic development projects
- Participation in Public Programs/Loan Pools and Consortia
 - Small Business Administration Loans
 - Public/private loan pools and consortia
- Other Forms of Business Support
 - Loan review
 - Minority vending
 - Counseling and technical assistance

Consumer Loans

Farm Loans

Building Community Capacity

- Support for Community Development Credit Unions
- Support for Community Development Loan Funds
- Loans and Credit Lines to Community Development Corporations
- Grants to Community-Based Organizations

Banking Services, Branch and Staff Policies

- Banking Services
 - Offer basic or lifeline checking
 - Cash government checks
- Branch Policies
 - Commitments to keep bank branches open in selected neighborhoods
 - Commitments to open new branches
- Bank Staff and Structure
 - Hiring policies
 - Bilingual staff
 - Train bank staff
 - Diversify board

Needs Assessment, Marketing and Outreach, and Accountability to the Community

- Credit Needs Assessment
- Marketing and Outreach
 - Advertising
 - Seminars and training
 - Create new CRA position
 - Call programs
 - Marketing through community groups
 - Create a special unit
- Accountability and Community Participation
 - Review board
 - Reports and disclosure

CRA agreements to minority and low-income households and census tracts. The analysis drew on two data sources: national mortgage lending data for 1994 provided through the Home Mortgage Disclosure Act (HMDA)² and a comprehensive national listing of CRA agreements compiled by NCRC (1996). The analysis used two indexes of mortgage lending activity. The first index compares a lender's share of total mortgage approvals in a given metropolitan area or state³ for a particular type of household or census tract (e.g., African-American) to its share of total mortgage approvals in that same metropolitan area or state. The index shows the extent to which a lender's mortgage approvals for a particular population group are proportional to its market share of total mortgage approvals.

The second index compares a lender's mortgage denial rate for low-income and minority households and census tracts to its denial rate for high-income and white households and census tracts. This index shows the extent to which a lender's denial rate to disadvantaged population groups and communities deviates from its denial rate for the most advantaged groups and neighborhoods.

The market share analysis revealed that banks with agreements were significantly more responsive than other lenders to the credit needs of low-income and minority households and census tracts. For banks with agreements, their market share of mortgage approvals for minority and low-income households and census tracts exceeded their overall market share of mortgage approvals within that state or metropolitan area. In contrast, minority and low-income households and neighborhoods represented a significantly smaller proportion of the total market share for banks without agreements. For example, whereas banks with agreements posted an average market share index of 1.12 for African-American households (indicating that their share of mortgage approvals for African Americans was 112 percent of their share of total mortgage approvals), the score for other banks was only 0.72 (see table 2).

In contrast with the market share index, few significant differences were found in the denial rate indexes of lenders with and without

² In 1975 Congress passed the Home Mortgage Disclosure Act, which requires banks and other lenders to disclose to the public data on the location of their mortgage loans. HMDA's disclosure requirements have been extended several times since the law's original enactment. In 1989 Congress amended HMDA to require banks to disclose for the first time data on the racial and socioeconomic characteristics of all loan applicants and the outcomes of their applications (see Fishbein [1992] for a review of HMDA's evolution).

³ When every agreement in a state was statewide in scope, the index covered statewide market shares. If one or more agreements applied to a metropolitan area or to a smaller geographic area, the index was pegged to metropolitan market shares.

Table 2. Index of Bank Shares of Total State/Metropolitan Statistical Area Mortgage Approvals

	Index Mortgage Approvals			F Statistic
	Total	No Agreement	Agreement	
Household Race				
White	1.03	1.03	0.99	23.59**
Minority	0.81	0.77	1.12	89.24**
Black	0.77	0.72	1.18	71.09**
Hispanic	0.83	0.79	1.16	36.02**
Other	0.88	0.86	1.00	6.99**
(n)	3,851	3,378	473	
Household Income				
Low-income	0.80	0.78	0.92	4.68*
Moderate-income	0.98	0.95	1.18	31.28**
Middle-income	0.93	0.92	1.00	13.48**
High-income	1.04	1.04	1.00	12.04**
(n)	3,854	3,381	473	
Tract Race				
Low-minority tracts	1.00	1.00	0.98	4.14*
Moderate-minority tracts	0.88	0.84	1.15	17.36**
High-minority tracts	0.82	0.75	1.30	38.44**
(n)	3,827	3,355	472	
Tract Income				
Low-income tracts	0.96	0.90	1.40	25.60**
Moderate-income tracts	1.08	1.06	1.19	4.59*
Middle-income tracts	1.01	1.01	0.98	2.42
High-income tracts	0.95	0.95	0.94	0.07
(n)	3,830	3,357	473	

Note: Analysis excludes independent mortgage banks and banks with fewer than 30 mortgage approvals.

*Significant at 0.01 confidence level.

**Significant at 0.05.

agreements. Only for African-American households was there a significant difference, with banks with agreements posting a denial index of 2.5, compared with 3.13 for banks without agreements. In other words, banks with agreements denied mortgages to African-American applicants 2.5 times more often than to whites whereas other banks denied mortgages to African-American applicants 3.13 times more often.

The study also compared the lending of banks with different types of agreements. It examined the market share indexes of banks with voluntary versus negotiated agreements; with agreements signed in different years; with agreements having different geographic scopes (city, state, national); and with agreements involving groups with varying amounts of experience in negotiating CRA agreements. Few significant differences were found among banks with different types of agreements. Regardless of their voluntary or negotiated status,

age, geographic coverage, or number of additional agreements signed by the same community group, banks with agreements consistently posted market share indexes of 1.00 or higher.

The first article looked only at home purchase mortgages and home improvement loans (the latter not reported here); it did not examine other types of bank loans and services that are often contained in CRA agreements. Moreover, it did not assess the extent to which banks attained the specific mortgage lending goals of their CRA agreements. This article takes a closer look at the agreements struck by community organizations and local government in four places with multiple agreements—Chicago, Cleveland, New Jersey, and Pittsburgh. It examines how CRA agreements are monitored and enforced and discusses their effectiveness. The case studies are based on interviews with representatives of the banks, community groups, and other organizations that negotiated the agreements, as well as others involved in the implementation of the agreements, such as government officials, community development corporation (CDC) executives, real estate agents, and minority business organizations. In addition to interviews, the case studies draw on the text of the agreements, newspaper articles, reports, and other relevant documents.

Not only do the case studies help document the achievements of the CRA agreements, but they also help explain the successes and shortcomings of the agreements. The case studies consider, for example, the mechanisms established to monitor the agreements, the organizational culture of the institutions that negotiated the agreements, and the relationship between the banks and the community organizations that signed the agreements. The case studies compare differing strategies for furthering CRA goals and variation in the objectives of the agreements.

Chicago, Cleveland, New Jersey, and Pittsburgh are among the nation's most active areas in the CRA arena. Banks in these four areas have negotiated more than 50 agreements totaling more than \$8 billion, involving a variety of loans, investments, grants, and other commitments. The experiences in these four places shed light on both the accomplishments and limitations of CRA agreements.

Overview of agreements

The agreements in the four sites were negotiated and monitored by a variety of organizations. In New Jersey, the lead organization was New Jersey Citizen Action, a statewide, grassroots advocacy group. In Pittsburgh, it was a coalition of neighborhood organizations. Chicago also featured a coalition of community-based organizations,

but one that was considerably less formal than Pittsburgh's.⁴ Cleveland is one of few places in the nation (Denver is another) where the municipal government has led CRA challenges; it is far more common for advocacy groups, community-based organizations, and coalitions to mount such challenges.⁵

Every agreement involves home purchase mortgages. Many also call for increased lending and investment for affordable housing development and for minority-owned businesses. In addition, the

⁴ The Chicago agreements covered in this article involve three of the city's largest banks: First Chicago, Northern Trust, and Harris Trust and Savings Bank. The agreements were first negotiated in 1984 by an ad hoc coalition of community organizations and advocacy groups that called itself the Chicago Reinvestment Alliance. The Alliance instituted the Neighborhood Lending Program (NLP) as a set of customized lending goals for home mortgages, multifamily housing development, and business lending. The Alliance also organized separate community advisory committees to monitor each bank agreement. The Alliance had dissipated by the late 1980s, although most of its original members remain active in the CRA field and the community advisory committees continue to operate. In 1989 the three banks renewed the NLP. A new set of agreements were forged in 1995, including one with First Chicago and NBD, a large Detroit-based bank that First Chicago was merging with. The original advisory committees continue to monitor the newest agreements. Northern Trust, in addition to its participation in the NLP, developed a strategic plan to replace standard evaluation criteria for use by federal regulators in its CRA evaluation. Northern Trust is one of the first major banks to elect the strategic plan option; in many respects, the strategic plan's language and terms resemble that of a negotiated CRA agreement.

It should be pointed out that the case study does not cover all of Chicago's CRA agreements. ACORN (Association of Community Organizations for Reform Now), for example, has negotiated agreements with several Chicago banks. Unlike the others, the ACORN agreements do not put forth specific financial targets and are usually limited to home purchase mortgages. The agreements require the banks to modify their mortgage underwriting standards and to accept applications referred to them by ACORN's mortgage lending counselors. Besides ACORN, several neighborhood organizations have also negotiated relatively small, sometimes informal, agreements with neighborhood-based lenders.

A final note on the Chicago case: The article does not cover an agreement struck in 1998 between a large coalition of community groups and reinvestment advocates and First Chicago NBD in advance of the bank's merger with BancOne.

⁵ Cleveland's series of bank agreements was sparked by the election of Mayor Michael White in 1989. Soon after his election, the mayor asked the city's director of Community Development, who was a former community organizer and community development corporation leader, to develop a strategy based on CRA to make banks more supportive of Cleveland's community development efforts. Staff from the Department of Community Development met with community groups to establish the provisions that any bank agreements should include. These provisions were to include home mortgages, home improvement loans, housing development financing, small business lending, and a mechanism to monitor the performance of the agreements. In 1992 the city launched its first CRA challenge to a proposed bank acquisition; two years later, it had negotiated agreements with seven banks, including most of the city's largest lenders.

agreements often include commitments to retain and/or open new bank branches in underserved communities and provide grants and/or loans to community-based organizations. Some agreements call for specialized loan products, including below-market-interest-rate mortgages. Some also seek to increase minority employment within the banks. Finally, the agreements in New Jersey and Pittsburgh also require the banks to provide grants to the groups that negotiated the agreements. In New Jersey, the grants help support New Jersey Citizen Action's network of loan counseling offices. In Pittsburgh, the grant helps support the Pittsburgh Community Reinvestment Group (PCRG) staff.

Unlike the agreements in Chicago, Cleveland, and New Jersey, which set forth specific financial goals for various categories of lending, investment, and grant making, only one of Pittsburgh's agreements, its first, includes such provisions. PCRG struck its first agreement in 1988 with Union National Corporation (UNC), which had proposed to merge with another institution and create a new bank holding company, Integra Financial Corporation. Much to PCRG's surprise, UNC acceded to the group's initial demand for \$109 million in loans over a five-year period. PCRG arrived at this amount through a community needs assessment and expected it to be spread among several bank agreements. However, UNC decided to take a risk by agreeing to PCRG's entire demand because they considered PCRG a partner that would help them achieve their lending goals (Metzger 1992).

After UNC agreed to meet PCRG's entire needs assessment, the group decided to place more emphasis in its subsequent agreements on developing strong relationships with banks. The objective of these relationships has been to show progress in the following areas: (1) establish ongoing regular meetings with bank officials, (2) participate in a credit counseling initiative, (3) increase community outreach efforts, (4) increase the diversity of bank employees, (5) utilize below-market-rate funds, (6) work to create effective procedures for disposition of properties located in low- and moderate-income neighborhoods, and (7) provide PCRG with a grant for operating support. PCRG decided that pursuing a set of goals rather than specific numeric targets would be less time-consuming to monitor, would give it more flexibility in developing strategies to achieve these goals, and would enable it to expand the scope of what were considered CRA issues (i.e., increasing the diversity of bank employees and use of subcontractors). Subsequent agreements were negotiated with 11 additional Pittsburgh banks based on this new approach. In general, bank officials viewed their agreements with PCRG as working documents rather than as rigid business plans and were also more comfortable with the absence of specific

numeric targets because it allowed them more flexibility in fulfilling their CRA commitment.

Three sites used formal or informal coalitions to set the terms of their agreements. In New Jersey, Citizen Action worked with a statewide coalition of community development organizations and the leader of the African American Chamber of Commerce to develop the terms of community development (mostly rental housing development) and small business lending. In Chicago, several advocacy and community-based organizations formed an ad hoc coalition, the Chicago Reinvestment Alliance, to negotiate agreements with three large banks. PCRG in Pittsburgh is a coalition of about 27 neighborhood organizations (originally 15) founded in 1988 to protest a bank merger. As a condition of membership, neighborhood organizations must pay annual dues and participate in at least half of the total meetings held each year by two bank community advisory committees. In Cleveland, the city established a negotiating team for each agreement. The team consisted of the directors of the city's departments of Community Development and Economic Development and a representative from the city's Law Department. Staff support was provided by the Department of Community Development.

Monitoring and enforcement

All four sites rely on networks of community development organizations, advocacy groups, business associations, and other groups to help monitor the implementation of their agreements. Typically, the sites form community advisory committees,⁶ with members selected by the community organizations and usually the banks. Committees meet on a regular basis, usually quarterly or semiannually. Their members review the progress made by the banks in meeting their lending and other goals, discuss problems that have emerged, and suggest ways to improve marketing and community outreach. Although similar in form, the advisory committees differ across the four sites in the level and type of follow-up given to the meetings and the general level of satisfaction with the meetings and their outcomes.

Advisory committees. In Cleveland, the city forms a community advisory committee for each bank agreement. These committees include the directors of the city departments of Community Development and Economic Development, bank representatives, and

⁶ In Chicago, these committees are called review boards; in Cleveland, advisory committees; in New Jersey, community advisory councils; and in Pittsburgh, community development advisory groups.

representatives of nonprofit neighborhood groups. Typically, the committees meet twice a year, once in the spring (after the release of the latest HMDA data) and once in the fall. At the advisory committee meetings, the bank presents a breakdown of loans by neighborhood area for each major category (home mortgage, small business, etc.) After the spring meeting, each committee writes a report to the mayor describing the bank's progress in reaching the agreements' goals. Some of these goals concern the amount of money loaned or invested in specific areas. Others involve discrete actions, such as the hiring of an additional mortgage originator for the city of Cleveland or the preparing of a marketing plan or a minority hiring plan.

The committees' primary responsibility is to report on the progress made in achieving the objectives described in the bank agreements. Their second responsibility is to make recommendations for mayoral action, if such action is deemed necessary. For example, a report may suggest that the bank change its underwriting standards or extend the terms of the loans. It may suggest ways to reach particular markets, such as minority-owned businesses. At least one report suggested that the bank qualify itself to issue Small Business Administration loans. More than once, reports have recommended that the mayor write a bank's CEO, "putting it on notice" about a weak area of performance. In addition to the advisory committees for each agreement, the city also convenes a "neighborhood reinvestment committee" that meets annually or "as needed." This committee includes at least one representative from each community advisory committee and looks broadly at the city's bank reinvestment program and lending activity. It recently standardized the way agreement progress is reported back to the mayor and is now developing uniform reporting requirements for the banks.

The city also holds public meetings to discuss bank service issues. It mails invitations to an extensive list of community organizations, residents, businesses, nonprofit and for-profit housing developers, and public officials. It uses the meetings to solicit input regarding experiences with banks and to discuss the city's bank agreements.

Chicago pursues a similar procedure, holding regularly scheduled meetings with each bank. However, the tone and substance of the committee meetings differ markedly from bank to bank. One bank follows a tightly structured format, using *Robert's Rules of Order* to guide its discussions. Another bank committee is much more free-wheeling and confrontational in the discussions between bank and community representatives. A third is more sedate and focuses at least as much on broader policy issues in housing and community development as on the performance of the agreement.

In New Jersey, committee meetings tend to be one-sided, with the banks reporting on the progress of their agreements, but with minimal questions or discussion afterwards. Although the agreements require a formal reporting process for monitoring agreement implementation, most of those interviewed do not regard the bank reports or the community advisory councils as particularly effective. Officials of Citizen Action and its allied organizations assert that it is difficult to verify—or sometimes even interpret—what the banks report. Data may not be presented in a readily accessible format and even when they are, they can be difficult if not impossible to verify. Part of the problem is that Citizen Action lacks the staff necessary to analyze bank reports. In addition, several respondents said that banks are seldom questioned at the community advisory council meetings, perhaps because representatives do not know what questions to ask—that is, how to interpret the data the banks present. Also, some advisory council members may be reluctant to strain their relationship with the bank by asking tough questions. This may be particularly true of CDCs, which may be cautious about confronting banks for fear of damaging their relationships with these lenders. One exception in this regard is the president of New Jersey's African American Chamber of Commerce, who had helped Citizen Action formulate the small business provisions of its agreements. He sits on three advisory committees and has been aggressive in monitoring the banks' business lending and in helping the banks improve their marketing and outreach to the minority business community. He attributes his willingness to challenge the banks to the fact that he did not have any preexisting bank relationships to protect.

In Pittsburgh, the agreements' community development advisory groups (CDAGs) play a dominant role in monitoring bank performance and in nurturing a working relationship with the banks. As these relationships evolve over time, the nature of CDAG meetings often shifts from confrontation to collaboration. The primary issues discussed at CDAG meetings include (1) developing new lending initiatives, (2) employment and outreach strategies, (3) legislative and regulatory changes to CRA, and (4) a mortgage credit counseling program. Each CDAG is chaired by a PCRG member and includes bank officials and PCRG members. Most CDAGs meet monthly, but a few meet bimonthly and one meets quarterly. Prior to each CDAG meeting, PCRG members set an agenda of issues they wish to raise and generally outline them in a letter sent to bank officials. Participating banks also hold pre-CDAG meetings and send a letter describing their list of priorities, taken as a sign of how seriously they view CDAG meetings. In addition to pre-CDAG meetings, PCRG holds monthly membership meetings to provide representatives an opportunity to be candid about their concerns,

develop strategies for future actions, provide an update on progress, and exchange ideas and information.

Other types of monitoring. In addition to what the banks report at advisory committee meetings, reinvestment advocates monitor bank lending on their own. In Pittsburgh, Chicago, and Cleveland, staff analyze HMDA data to track changes in mortgage lending activity. In Pittsburgh, PCRG publishes an in-depth analysis, titled *Follow the Money*, of mortgage lending by the banks with which it has agreements (PCRG 1995). Chicago's Woodstock Institute annually publishes a comprehensive analysis of the lending in Chicago by all banks, mortgage banks, and thrifts covered by HMDA (Woodstock Institute 1997). The Woodstock report lists the number and dollar amount of mortgages for single-family and multifamily structures and home improvement loans made by each lender in each of Chicago's 77 community areas. The city of Cleveland also analyzes HMDA data but does not publish the results. In New Jersey, Citizen Action does not regularly analyze HMDA data to monitor bank lending; at the time of the case study, Citizen Action lacked the necessary staff for this analysis, although it had occasionally received technical assistance from local universities to help analyze lending data. It usually learns of problems when it receives complaints from prospective home buyers that banks are either turning down their mortgage applications or channeling them to higher-cost conventional mortgages. Citizen Action's statewide network of 16 loan counseling offices refers New Jersey residents to banks that have signed agreements with Citizen Action. Loan counselors routinely ask clients to report back on the outcome of their mortgage application, thus alerting Citizen Action to possible infringement of its agreements.

In addition to gathering resident complaints, Citizen Action conducts its own investigations of agreement compliance through what it calls "mystery shopping." Citizen Action staff and volunteers telephone the banks to inquire about available mortgage terms. Citizen Action instructs the "shoppers" to play out a specific scenario each week. One such scenario is as follows:

A single parent with two children. Income of \$24,000 per year. Hoping to buy in an urban area. The caller states that she has been a licensed practical nurse (LPN) at a local urban hospital for three years. She had a previous credit problem while in school to become an LPN. She is nearly certain she has cleared up her credit, but hasn't seen a recent report.

Citizen Action compiles and analyzes the results of the mystery shopping to see what type of mortgage information, if any, is pro-

vided, including the mortgage products specified in the bank's CRA agreement with Citizen Action.

When Citizen Action receives significant numbers of complaints about a specific bank or if mystery shopping suggests that banks are not promoting their discounted mortgages, Citizen Action's executive director will request a meeting with the bank's president to discuss the problem.

Impacts of agreements

The reinvestment agreements at all four sites yielded mixed results. Because they cover a variety of products and activities, not just single-family mortgages, it is not surprising that some aspects of the agreements are more successful than others. This assessment of the agreements' performance is based primarily on interviews with the community organizations and banks and other participants in the agreements and their advisory committees. With few exceptions, numerical data were not available to document agreement compliance. HMDA provides only partial insight into the agreements' performance, because it covers only single- and multi-family lending and none of the other areas included in the agreements, such as business loans, equity investment in multifamily housing, grants to community organizations, and branch bank operations. Furthermore, HMDA does not indicate the terms of the mortgages and therefore cannot be used to monitor the extent to which banks provide the specific products called for in the agreements, such as discounted interest rates, higher-than-usual loan-to-value ratios (LTVs), no PMI, and so on.

In general, the agreements seem most successful in meeting their lending targets for single-family home mortgages. Banks and community organizations alike state that banks have improved their mortgage lending to low-income and minority households and neighborhoods. The results are more uneven for construction loans, permanent financing for new housing development, and business loans. Results are more uniformly positive with regard to grant making to community organizations, investments in new housing development, and maintaining and operating inner-city bank branches. Beyond their specific terms, the agreements have in most cases also helped foster new, mutually beneficial, relationships between banks and community groups.

Single-family mortgages

Home purchase mortgages, as noted earlier, are the common denominator of most CRA agreements. Virtually all agreements con-

tain provisions for mortgage lending for single-family homes. At all four sites, banks have usually reached or surpassed their mortgage lending goals in most years for homeowner housing. For example, the 12 Pittsburgh banks with CRA agreements increased their total number of loans to African Americans by more than 200 percent from 1991 to 1994; their mortgage approval rate for African Americans increased from 28 percent to 62 percent (PCRG 1995).⁷

When banks fail to reach their lending targets for single-family mortgages, it is usually the case that rising interest rates have reduced the volume of mortgage applications. Although lending to minority and low-income households and neighborhoods has generally increased, some respondents, especially in New Jersey, argue that banks do not always vigorously promote their CRA products. At times they steer applicants to conventional mortgages that involve higher transaction costs (points), PMI, and higher interest rates.

Other products

Community representatives are generally less satisfied with the performance of the agreements' provisions involving loans for small businesses and real estate development. Most state that banks often fail to reach their lending goals in these areas. Groups also state that the nature of these products makes it more difficult to monitor and enforce these aspects of the agreements. In particular, because lending for real estate development and small businesses is far less structured and standardized than for single-family mortgages, assessing a bank's decision to reject particular loan applications can prove difficult (DiPasquale and Cummings 1992). It is hard for community advisory committee members to determine whether loan applications are turned down because of the applicants' failure to meet legitimate credit standards or because the bank failed to give the applications sufficient attention. It may also be difficult to ascertain whether loans that are approved by the

⁷ In Cleveland, one respondent claimed that the city's CRA agreements have caused mortgage banks to lose market share to the participating banks. Before the agreements were signed, he said, mortgage banks accounted for the bulk of the city's mortgage originations. Now, the mortgage banks' grip on the city's mortgage market has weakened as the CRA agreements have prompted major commercial banks to offer mortgages at more favorable terms. However, an analysis of HMDA mortgage lending data for the 1992–95 period failed to support this contention. Independent mortgage banks maintained a steady share of the metropolitan area's mortgage originations—overall and in predominately low-income and minority neighborhoods.

banks should necessarily be counted toward the agreements' lending targets—that is, whether real estate and business loans are actually benefiting low-income or minority households and communities.

Chicago probably has had more success in both real estate and business lending than the other sites, although outcomes vary from bank to bank. The Chicago agreements originally designated certain community-based organizations to serve as “loan packagers” for business and real estate loans. Staff at those organizations served as intermediaries between community groups and business owners and the banks. As loan packagers they collected all of the information necessary for completing the loan applications. At times they provided extensive technical assistance, conducting feasibility studies, selecting sites, and overseeing the development process (Bradford 1989, 22). Although loan packaging did not ensure bank approval of all loan applications, it did give the participating organizations direct knowledge of the merits and the credit risks of the loan application. However, the banks and community groups eventually decided to have the banks initiate business and real estate loans on their own in order to increase the volume of loan production. Even so, most direct loans were required to have the explicit endorsement of a community-based organization to show there was “support for the purposes of the loan in the community” (Bradford 1989, 28).

Investments, grants, branch operations, and other provisions

Little difficulty was reported at all four sites in reaching the agreements' goals for investment in low-income tax credits and for grants and loans to community organizations. In New Jersey and Cleveland, the agreements called for banks to invest in multifamily rental developments that received LIHTCs. Citizen Action and the City of Cleveland viewed the agreements as a way to expand the market for tax credits and increase the availability of equity capital for low-income housing development. Once the banks became familiar with the tax credit program, they have consistently met or exceeded their agreements' goals for tax credit investment.

The banks have also consistently met their agreements' goals in grant making. In New Jersey and Pittsburgh, the CRA agreements require banks to provide operating support for the organizations that signed their CRA agreement. In New Jersey, bank funds help support Citizen Action's mortgage counseling offices. In Pittsburgh, they help underwrite staff salaries at PCRG. In Cleveland, the agreements encourage banks to provide grants and lines of credit to community-based organizations. These goals are usually achieved.

Several agreements also contain terms relating to the retention and creation of branch banks in inner-city neighborhoods. Agreements variously pledge not to close existing inner-city branches or to open additional such branches. Surprisingly, in a time when technological change (automatic teller machines [ATMs]) and organizational change (bank mergers) have led numerous banks to reduce their branch operations (Avery et al. 1997), this has not been true of the banks with CRA agreements.⁸ Banks in Cleveland, Chicago, and Pittsburgh have kept existing branches open and in some cases opened new ones. Cleveland has not lost a single inner-city branch at any of the banks with which it has agreements. The same is true in Chicago. Contrary as it is to prevailing trends, this may also reflect the fact that many inner-city neighborhoods have long been deprived of branch banks. Unlike middle-income areas, which now often have a surfeit of branches—which banks are now cutting back—CRA agreements have demonstrated to the banks that low-income urban areas are “underbranched” and can support new branch operations.⁹

Some agreements also aim to influence the bank’s hiring and procurement processes. In Cleveland and Pittsburgh, the agreements call for the banks to increase their employment of minority staff and in some cases to increase their purchasing from minority-owned businesses. Neither element has proved to be especially successful. In Cleveland, the city has given much less emphasis to bank hiring practices than to bank lending and service delivery, in part because it is not sure if CRA gives the city legal standing to force banks to change their employment or procurement procedures.

Partnerships and rediscovery of the inner city

In Cleveland, Chicago, and Pittsburgh, banks and community groups credit their CRA agreements with helping banks “rediscover” the inner city as a viable and profitable market. The agreements and the resulting partnerships have helped the banks better

⁸ According to a recent study by the Federal Reserve, the number of central-city bank branches declined by 10 percent from 1985 to 1995 (and branches in low- and moderate-income central-city neighborhoods fell by 22 percent). During the same period, suburban branches posted a slight gain of 1.5 percent (although branches in low- and moderate-income suburban neighborhoods decreased by nearly 14 percent) (Avery et al. 1997, 720).

⁹ The Federal Reserve study referred to in footnote 8 also shows that central-city neighborhoods have fewer bank branches than suburban and rural areas in the same income categories. For example, while moderate-income (50 to 80 percent of area median) ZIP Code areas in central cities had 2.08 bank offices per 10,000 residents in 1995, the corresponding ratios for suburban and rural ZIP Code zones were 3.07 and 4.39, respectively (Avery et al. 1997, 720).

understand the inner-city market for mortgages and other financial services and to develop products and marketing strategies to serve it. In Cleveland, several bank officers said that the suburban mortgage market had become “saturated” and that the central city provided untapped demand for mortgage loans. Respondents in Chicago also claimed that bank agreements helped the banks recognize a new market in “mixed-use buildings”—structures with retail space on the first floor and residential units above. This building type is very common in Chicago neighborhoods but had been neglected by the mortgage industry. Several agreements set goals for mixed-use mortgages. According to the respondents, the agreements helped fill critical gaps in the Chicago mortgage market. In Pittsburgh, too, several banks credited their partnership with PCRG with having helped them improve their business in the inner city.

More broadly, many (but not all) participants say the agreements fostered productive partnerships between banks, community groups, and local government. Through advisory committee meetings, the participants become more familiar with each other’s strengths and limitations. Banks saw how community-based organizations offer access to residential and commercial markets that they would otherwise be hard-pressed to tap. Community groups may also help the banks better appraise the risks involved in inner-city lending. The partnerships give community groups a stronger understanding of the parameters that shape a bank’s capacity to increase its lending and change underwriting standards and practices. At times, community groups also gain an ally in the banks in their quest for government grants or contracts and in their lobbying efforts.

The partnerships also manifest themselves outside the immediate framework of specific agreements. For example, once banks become more knowledgeable about the activities and capabilities of CDCs as a result of their participation in implementing CRA agreements, they sometimes become much more aggressive in offering loans and other services to these organizations. In Cleveland, several CDC executive directors said that before their involvement in CRA agreements, banks were highly reluctant to consider their loan applications—indeed, loan officers rarely returned their phone calls. Now, banks frequently call them, loans at the ready. Moreover, banks and community partners collaborate occasionally to lobby legislatures and government officials at the local, state, and federal levels.

CRA agreements have also helped strengthen connections between banks and government. In Cleveland, the city has used its agreements to help capitalize a new microlending loan pool for new businesses. In Pittsburgh, the agreements encourage the banks to util-

ize low-interest funds provided through the Federal Home Loan Bank Board's Affordable Housing and Community Development programs. Banks use these funds to provide grants and low-interest loans. Of course, not all agreements produce congenial partnerships. Some groups, such as ACORN (Association of Community Organizations for Reform Now), try to avoid becoming too close with the banks they have agreements with, in part to avoid becoming co-opted. In New Jersey, some bank agreements have produced more trust and cooperation among the participants than others. In some cases, bank officials work closely with Citizen Action and its allied community organizations, but relations remain tense in others.

The emergence and development of new relationships between banks and community groups bring to mind the concept of social capital.¹⁰ In the process of negotiating and then monitoring CRA agreements, bankers and community advocates “come to the table.” At first they come as antagonists. Over time, however, the character of their relationship may change as bank and community representatives become better acquainted and begin to understand each other's strengths and constraints. In short, the monitoring process can foster a sense of trust, reciprocity, and common interest—hallmarks of social capital (see Keyes et al. 1996)—between bank and community. On the other hand, formation of social capital is by no means inevitable, as some relationships remain more adversarial than others. Moreover, seemingly harmonious relationships can turn bitter—for instance, in the aftermath of a bank merger or when the goals and priorities of a partner change.¹¹ If social capital

¹⁰ For a discussion of the relationship between microlending and social capital, see Servon (1998).

¹¹ An agreement between a neighborhood group in Chicago's far south side and a local savings bank provides a cautionary tale about the fluid character of relationships forged from CRA agreements. In 1988 one community group signed a three-year, \$20 million agreement after an intensive campaign. The agreement authorized the community-based organization to provide mortgage counseling for neighborhood residents and to refer qualified applicants to the bank for pre-approved mortgages. To facilitate mortgage counseling, the bank furnished the community group with a “credit check machine.” Just nine months after the agreement was signed, the bank and community group had reached their three-year goal for mortgage lending. The bank approached the community group and said there was no need for additional agreements—“that we can do business now.” The bank promised to put more money into the program without a formal agreement. Together they held a press conference to publicize the success of their partnership and that it was “good business doing business in the community.” The relationship worked well for the first three years. It began to fray, however, after the bank's presidency turned over. At this time, the community group convened a “community review board” consisting of three representatives from the community and three from the bank to monitor the program. In the early 1990s, other banks increased their profile in the community, increasing the level of competition in mortgage and

emerges from the implementation of CRA agreements, it is not necessarily self-perpetuating and must be exercised to survive.

Lessons learned

The case studies of CRA agreements in Cleveland, Chicago, New Jersey, and Pittsburgh yield several lessons regarding the possibilities and limitations of those agreements. As reported in the previous section, the agreements seem to produce real changes in lending practices, at least at some banks and in some areas. This section looks at the conditions that seem to make these changes possible and at several factors that stand to constrain the implementation of agreements in the future.

The need for staff

Less important than the terms of the agreements themselves is how the agreements are implemented, monitored, and enforced. At a minimum, the groups that negotiate and oversee agreements need the capacity to monitor their compliance. This requires staff to analyze HMDA data and examine the periodic reports submitted by the banks. These reports generally cover the entire scope of an agreement, including such areas as small business lending that are not covered by HMDA. Staff need to compare the bank reports over time to identify trends in agreement compliance. They may also need to draw on the reports to pose questions to the banks and the advisory committees for improving their performance. In addition to HMDA data and bank reports, staff may also need to study the banks' CRA statements and evaluations. Without adequate staff, organizations lack the capacity to monitor or enforce their agreements.

small business lending. The bank started pulling back and showed increased interest in suburban residential markets. It downsized its neighborhood office and relocated its commercial lending and mortgage departments to a suburban office. In 1995 the bank terminated the community group's mortgage counseling operation and took back the credit check facility. That same year the bank said there was no purpose in continuing the community board meetings because the community group was not generating significant business for the bank.

This episode shows that relationships between banks and community groups can be transitory. In this case, the relationship deteriorated when the bank changed its market focus from the city to the suburbs and decided that its relationship with the community group no longer generated sufficient returns to be worthwhile and (perhaps) that the community group lacked the clout to penalize the bank for terminating the partnership.

Of the four sites, three employ at least one staff person to monitor the performance of the agreements. In Cleveland and Pittsburgh, the lead organization (the city of Cleveland and PCRG, respectively) employs someone to monitor bank performance. In Chicago, this function is carried out by two organizations. National People's Action compiles quarterly and annual reports (with financial support from the City of Chicago) to assess the performance of several agreements. The Woodstock Institute, as noted previously, reports on mortgage lending throughout Chicago by all banks, whether or not they have CRA agreements. Although the Woodstock reports are not specifically connected to any agreements, they provide a continual accounting of bank lending practices. New Jersey is more sporadic in its monitoring and assessment of agreement performance. As noted above, it does not always have staff available to examine HMDA data or bank reports. At times, other organizations have conducted studies for Citizen Action. Furthermore, volunteers periodically go mystery shopping to check that banks are referring potential home buyers to the mortgage products specified in the agreements. Citizen Action's network of mortgage counseling offices also helps monitor the performance of the mortgage lending components of the agreements.

Organizational structure

Banks implement their CRA agreements in different ways. At one extreme, the products called for in the agreements are handled exclusively by the banks' community reinvestment department—or its equivalent. Bank personnel at branch offices and other units of the banks are not aware of the agreements' content. At the other extreme, banks make a concerted effort to integrate the handling of the agreements throughout their organization. Loan officers are informed about products and underwriting standards specified in the agreements and are positioned either to accept applications for the agreements' loan products or to make referrals to the appropriate unit.

When a single unit, such as the community reinvestment department, takes sole responsibility for providing the products specified in the bank's CRA agreement, the staff are generally highly trained and motivated to deliver the product. They can provide superb service for the community groups and businesses that approach them for assistance. However, potential borrowers need to know where to go in the bank to obtain these loans, and they may not be aware of the products in the first place. On the other hand, when all bank loan officers are given responsibility for the bank's CRA products, personnel's knowledge, familiarity, and interest in these products can vary widely. Potential customers seeking loans may be treated

in quite different ways, depending on the particular loan officer they happen to see.

According to interviews with community representatives in Chicago, Cleveland, and New Jersey, the most effective arrangement is to require all bank branches to provide the agreements' single-family mortgages, but to assign loans for business and real estate development to more specialized units within the bank. Highly skilled staff can then become expert in the more specialized financial products for business and real estate, whereas responsibility for standardized home purchase mortgages can be broadly disseminated within the bank's organization. It remains crucial that loan officers throughout the bank be able to refer potential borrowers to the designated unit to apply for business or real estate loans. Bank management needs to take the agreements seriously.

The division of responsibilities for delivering CRA products is important for responding to customer inquiries. However, these internal arrangements matter little if the public is not aware of the agreements and the banks' loan products. Thus, marketing is central to the success of the agreements. Accordingly, marketing and community outreach are recurrent themes at bank advisory committee meetings. Both the banks and their community partners play a role in these efforts. For example, associations of community organizations may seek to inform their members of the existence and availability of the agreements' loan products.

Constraints

While the case studies show that at least some CRA agreements have stimulated bank lending to disadvantaged households and neighborhoods, they also illuminate several long-term limitations to the effectiveness of CRA agreements. Ironically, some of these limitations stem from the same sources that gave rise to most CRA agreements in the first place—the consolidation and restructuring of the financial service industry.¹² Bank mergers and acquisitions enabled community advocates to mount CRA challenges and motivated banks to launch voluntary reinvestment programs. Without these transactions, banks have little incentive and community groups little leverage to negotiate CRA agreements. However, mergers and acquisitions do not cease once a CRA agreement is signed. Numerous institutions have entered into agreements and then been

¹² After holding steady from 1975 to 1985, the number of commercial banks has since dwindled steadily. A Federal Reserve study shows a 13.9 percent drop of 2,005 banks from 1985 to 1990 and an 18 percent decline of 2,281 banks from 1990 to 1995 (Avery et al. 1997).

acquired by or merged with other financial institutions. For example, approximately one-third of the banks and thrifts listed in NCRC's 1996 inventory of CRA agreements no longer exist, mostly because of mergers and acquisitions.

It is not known what happens to a bank's CRA agreements after the institution goes through a merger or acquisition. CRA agreements are not legal contracts and do not appear to bind the acquiring institution to their terms. Sometimes the acquiring institution negotiates a new agreement or launches a voluntary reinvestment program that replaces any existing agreements. Other times all previous agreements become null and void.

In any case, mergers and acquisitions often bring changes in bank management or otherwise disrupt the relationships that had developed between bank executives and community leaders. It is common for the bank managers and officers that had negotiated and overseen their bank's CRA agreements to leave the bank, to be replaced by new managers who have had no previous relations with the groups that had signed the agreements and have little understanding or interest in the agreements. Even if managers are not replaced, their responsibilities and authority may be redirected or diminished. Decisions that used to be made within the bank may now be made externally by the parent organization.

The long-term stability of CRA agreements may depend on the bank's subsequent involvement in mergers and acquisitions and the role it plays in these transactions (as acquirer or acquiree, for example). In Cleveland, only one bank with a CRA agreement has so far been acquired by another institution. Fortunately for Cleveland, the acquiring institution made Cleveland its base of operations; decision-making authority was not transferred elsewhere and the acquiring institution honored the original CRA agreements and negotiated a new agreement later. At least one Cleveland bank with an agreement has taken over other institutions located elsewhere, including Integra in Pittsburgh, which had signed that city's first and largest agreement. Cleveland remains a regional banking center and has actually seen bank operations expand.

In Chicago, a Canadian bank corporation acquired Harris Savings and Trust, which has one of the city's three largest CRA agreements, but allowed Harris to retain most of its managerial autonomy and has not interfered with Harris's agreement. Of greater concern to Chicago's reinvestment advocates is a recent decision by the Bank of America to convert its Chicago subsidiary, Bank of America-Illinois (formerly Continental Bank) into a branch of its California-based parent. It is feared that this change will weaken the bank's commitment to its reinvestment goals and programs. In

1998 BankAmerica merged with NationsBank, which may further test the durability of the Chicago affiliate's CRA lending programs.

New Jersey has seen far more bank mergers and acquisitions than the other three sites. Many of the banks that Citizen Action had negotiated agreements with have been acquired by other institutions.¹³ Although Citizen Action usually negotiates new agreements with the successor institutions, the churning of the state's banking industry makes it difficult for Citizen Action and its community partners to develop and sustain relationships with individual bank officials.

New modes of delivering bank services present yet another challenge to the implementation of CRA agreements. As discussed earlier, banks with agreements have not replaced inner-city branches with ATMs; to the contrary, several banks have opened new branches. Nevertheless, banks increasingly use on-line computer systems and telephone services to take and process loan applications. Financial institutions are also turning to computerized "credit scoring" systems to evaluate loan applications. Although these systems streamline and accelerate the loan application process, they may reduce the banks' responsiveness to CRA agreements. Unless the terms of the agreements are explicitly programmed into the banks' automated lending systems, they could overlook the underwriting standards and loan terms that are specified in the agreements. Moreover, automation probably makes it more difficult for community advisory committees to monitor bank lending decisions. On the other hand, by reducing the labor costs of processing bank loan applications, automated underwriting may reduce a bank's bias against originating small loans and thus make it more receptive to loan applications from low-income households and small minority-owned businesses (Lea 1996).

Besides computerized lending systems, some banks are experimenting with other alternatives to traditional branches. For example, a major Chicago bank has partnered with a large grocery store chain to establish bank "counters" at selected supermarkets. These outlets are staffed by only one or two employees at any one time. Unlike full-service branches, these "bank counters" will provide only the most basic services, and their staff are unlikely to be fully versed in the terms of the bank's CRA agreements.

¹³ For example, PNC recently acquired Midlantic Bank and acquired most of Chemical Bank's New Jersey branches. First Union, which unlike PNC does not have an agreement with Citizen Action, acquired First Fidelity, which did. Most recently, Fleet Bank acquired NatWest, which had an agreement, and eventually signed a \$500 million agreement with Citizen Action.

The rising importance of the secondary mortgage market presents another constraint to the implementation of CRA agreements. Since the mid-1980s, most home mortgages originated by thrifts and commercial banks are sold to the secondary market. Heightened capital requirements imposed by the savings and loan bailout legislation of 1989 (the Financial Institutions Reform, Recovery, and Enforcement Act) limit the amounts of assets (loans) lenders can retain in portfolio relative to their capital. When banks do retain mortgages in portfolio, they usually favor adjustable-rate mortgages, which involve less interest rate risk than fixed-rate mortgages. Most mortgage products specified in CRA agreements are not easily transferred to the secondary market. Below-market interest rates, waivers of PMI, allowance of higher-than-usual obligation ratios (housing cost burdens), and other customized underwriting standards render these mortgages ineligible for purchase in the secondary market. As a result, the banks hold them in portfolio. While banks may retain their CRA mortgages in portfolio for a period of time, it will not be indefinite. There are limits to the amount of mortgages banks keep in portfolio. As this limit is approached, they will originate fewer and fewer mortgages of the types specified in their agreements. For example, a Cleveland bank dropped its waiver of PMI requirements in 1995, which caused the number of mortgage applications and approvals from minority and low-income households to decline.

At least two common features of the mortgages created by CRA agreements make them difficult to sell in the secondary market. "Discounted" (below-market) interest rates are one such barrier. In some instances, banks have informed the community groups that they will not include discounted rates in future agreements. More important than interest rates, which have been relatively low and stable since the late 1980s, is the issue of private mortgage insurance. The secondary market as a rule requires PMI on all mortgages if the LTV is greater than 80 percent (Munnell et al. 1992). Since virtually all mortgages specified in CRA agreements involve LTVs of at least 80 percent (i.e., down payments of less than 20 percent), mortgages without PMI must be retained in portfolio. Community groups feel strongly about the need to waive PMI. Otherwise, minority and low-income households and neighborhoods become vulnerable to any potentially discriminatory practices of insurance companies, which are not subject to CRA. Moreover, if PMI is required, banks with CRA agreements can always use a household's failure to obtain PMI as a valid reason for denying mortgage credit.

Starting in 1997, the secondary mortgage market seems to have become more receptive to loans originated to meet CRA goals. For example, after protracted negotiations with the National Training and Information Center and other community reinvestment advocates,

Fannie Mae launched an initiative to help depository institutions meet their CRA goals by securitizing or purchasing loans made to low-income households and borrowers living in low- and moderate-income neighborhoods. Fannie Mae uses several methods, including partially insured Real Estate Investment Conduits and bulk purchases of PMI, to securitize mortgages originated without PMI. Fannie Mae completed its first transaction under this initiative in August 1997 and by June 1998 had securitized nearly \$2 billion in CRA loans (Fannie Mae 1997, 1998). Other institutions also securitize CRA-related loans. For example, Access Capital Strategies LLC, a Boston-based financial service company, recently created a mutual fund to “act as a national secondary market for Community Reinvestment Act loans” (Brockman 1998). Initially capitalized with a \$25 million investment from BankBoston, the fund’s sponsors intend to acquire \$1 billion of loans over a one-to-three-year period. In April 1998, the Local Initiatives Support Corporation (LISC) announced plans to establish the nation’s first community development real estate investment trust (REIT). Among other kinds of investments, REIT will purchase loans originated by banks, community development financial institutions, and state and local housing agencies (LISC 1998).

Bank mergers and acquisitions, the appearance of new loan delivery mechanisms, and the imperatives of the secondary mortgage market may limit the ability of community groups to enforce their existing CRA agreements. Yet other developments pose still more fundamental concerns about the capacity of community organizations and local governments to negotiate effective CRA agreements in the future. In particular, the ongoing consolidation of the financial service industry, with individual firms enveloping commercial banks, mortgage banks, investment banks, mutual fund companies, and insurance companies, means that CRA will apply to an ever more narrow slice of the firms’ total operations.¹⁴ This concern was heightened by the announcement in April 1998 of the proposed merger of the Travelers Group and Citicorp. If the \$70 billion merger goes through, it would create an institution that would dwarf the nation’s other large financial institutions, combining in-

¹⁴ Several mergers of major financial institutions were announced in 1997 and 1998, including those of Morgan Stanley and Dean Witter (Truell 1997a), Travelers Group and Salomon, Inc. (Truell 1997b), Bankers Trust and Alex Brown (a Baltimore-based investment bank) (*Wall Street Journal* 1997). Short of complete mergers, other banks have acquired minority equity stakes in investment banks and other nonbank financial institutions. For example, PNC Bank recently announced its pending purchase of Friedman, Billings, Ramsey and Company, one of the nation’s fastest growing institutional brokerage firms. This investment supplements PNC’s previous acquisition of a retail stock brokerage firm and a capital markets business (Truell 1997c).

surance, mutual funds, investment banking, and consumer and corporate banking (Truell and Holson 1998).

Although commercial bank subsidiaries may remain subject to CRA, other financial subsidiaries will be beyond its reach. As a result, financial firms have increasing leeway to circumvent the spirit if not the letter of CRA. Financial institutions might promote the growth of their nonbank subsidiaries over their bank subsidiaries, thus shifting an increasing portion of their assets outside CRA's control. It is partly for this reason that community reinvestment advocates, as well as such federal regulators as the head of the Office of the Comptroller of the Currency, have proposed that Congress expand CRA to include additional financial industries ("House Banking Committee" 1997; "Ludwig Suggests Extension" 1997).¹⁵

Conclusions

Despite CRA's fractious history, there has been little published research on the performance of CRA agreements. The case studies presented here add to a small body of literature on the creation, implementation, and effectiveness of CRA agreements (see also Bradford 1989; Campden 1995a, 1995b; Ford and Carver 1996; Hamill 1990; Miara 1995; NCRC 1997; Schwartz 1998; Squires 1992). Much remains to be learned about the strengths and limitations of CRA agreements and their effects on communities and banks. Following are several key topics that warrant further investigation:

1. Comparison of negotiated and voluntary agreements. Large financial institutions increasingly establish voluntary reinvestment programs soon after announcing a merger or acquisition. Several of these agreements are national in scope and involve billions of dollars. Community reinvestment advocates, however, raise questions about accountability of these programs because banks are in control of their oversight. To date, there has been little if any comparison of voluntary and negotiated agreements, although Schwartz's (1998) analysis of HMDA data for 1994 found no significant difference in the mortgage lending patterns of banks with voluntary and negotiated agreements.

¹⁵ The House Banking Committee, for example, considered but ultimately rejected a proposal to extend CRA to nonbank financial institutions that would be permitted to affiliate with bank holding companies under a financial service reform bill (H.R. 10). However, the committee did create an advisory council to "examine the impact of new insurance and securities activities permitted to banks by the legislation on underserved communities and populations" ("House Banking Committee" 1997)

2. Analysis of the “strategic plan option.” The revised CRA regulations adopted in 1995 give banks the option of devising their own criteria for assessing their compliance with CRA. This strategic plan option replaces the standard definitions of the lending, investment, and service tests that bank regulators otherwise use to evaluate CRA compliance. The few strategic plans approved to date—including that of Chicago’s Northern Trust—closely resemble CRA agreements in terms of their goals and products. Moreover, the federal regulations require community input into the formulation of the plans. Unlike CRA agreements, which are not legally binding, strategic plans are monitored and enforced by bank regulators. It would be extremely interesting to compare the performance of these strategic plans with voluntary and negotiated CRA agreements.
3. Comparison of CRA agreements with other CRA-related activities. A third frontier for CRA research is to compare the loan products forged through CRA agreements with other programs and projects that banks may have created apart from specific agreements. It is important to distinguish the Community Reinvestment Act from CRA agreements. Although CRA applies to all depository institutions above a minimum asset size, CRA agreements involve a much smaller subset. Moreover, banks with and without CRA agreements often develop lending, investment, and service programs and strategies for low- and moderate-income households and communities that are not specified in any CRA agreement. It is therefore important to compare these other activities with those specific to CRA agreements.
4. Analysis of PMI approval process. As discussed above, the secondary mortgage market seldom purchases mortgages with high LTV unless they have PMI. However, community reinvestment advocates usually insist that banks waive their PMI requirements, which has forced banks to hold these mortgages in portfolio. Reinvestment advocates have been loath to allow PMI because private mortgage insurance companies are not subject to CRA and banks could use the failure to obtain PMI as a reason to reject loan applications from disadvantaged borrowers and neighborhoods. Although the secondary market has made several of its underwriting criteria more flexible—such as allowing higher debt-to-income ratios and permitting a broader range of income sources—mortgages without PMI seem to pose too much risk and uncertainty for the secondary mortgage market to tolerate. Studies of the mortgage application approval process—akin to Munnell et al.’s (1992) study of mortgage lending or matched pair tests—could do much to alleviate or confirm community reinvestment advocates’ fears about PMI.

The experiences in Chicago, Cleveland, New Jersey, and Pittsburgh suggest that CRA agreements improve bank responsiveness to urban communities. Besides home mortgage lending, banks seem most consistently successful in reaching their goals of affordable housing investments (tax credits) and making grants to community-based organizations. The record is more uneven and harder to assess for business and real estate development loans. At times the agreements have helped the banks reach new markets. Beyond their specific terms, the agreements seem to foster mutually productive relationships between banks and community groups.

The achievements of CRA agreements are fragile. Congress continuously entertains legislation aimed at weakening if not eviscerating CRA. The ongoing restructuring of the financial industry, including technological as well as organizational change, could undermine future agreements. Perhaps the most fundamental challenge is posed by the consolidation of once distinct financial specializations into a single industry—in particular, the merger of depository institutions, now the only ones subject to CRA, with other financial institutions that have remained outside CRA's control. Unless CRA is extended so that insurance, securities, and other financial services are required to serve low-income and minority communities, the law will apply to an ever-shrinking portion of a financial institution's business.

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