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PEOPLE OF COLOR HARDEST HIT BY THE FORECLOSURE CRISIS

Blacks and Latinos Were Unfairly Steered to the Subprime Market, and are More Likely to Have Higher Foreclosure and Loan Delinquency Rates

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Introduction

The foreclosure crisis has disproportionately affected African American and Latino communities, exacerbating existing economic inequality. African American and Latino subprime borrower losses due to foreclosure represent 46% of total losses to foreclosure, even as these two groups represent only 27.9% of the population of the United States. The loss of wealth African American and Latino subprime borrowers due to foreclosure is estimated at \$213.1 billion, compared to a loss of \$462.2 billion for subprime borrowers as a whole. (Rivera, et al., 2008)

Considering that the median household of color has \$0.15 for every dollar of White household wealth, the loss of wealth caused by the subprime mortgage crisis represents a significant portion of total wealth in Latino and African American households.

Steered into Subprime While Eligible for Prime

Latinos and Blacks were disproportionately the recipients of subprime loans, even when controlling for income and credit score. Among borrowers with the highest FICO

scores (720 or higher), 13.5% of Latino and 12.8% of African Americans received high-cost loans, compared to 2.6% of White borrowers with the same credit scores. (Federal Reserve Bank of San Francisco, 2009)

Additionally, 45.2% of Latino and 42.9% of African American borrowers received their loans from non-federally regulated independent mortgage companies, compared to 29.2% of Whites. (Federal Reserve Bank of San Francisco, 2009) Independent, unregulated mortgage companies are responsible for 75% of all subprime loans originated since 2000. (Testimony of Michael S. Barr, 2008)

Slipping out of the Middle Class

The present foreclosure crisis has not only laid bare the unjust racial foundations of our mortgage industry, but has also exacerbated existing disparities between Whites and their fellow Latino and African American citizens in terms of wealth creation. As of 2001, the median White American had financial assets of \$38,500, while the median person of color had median assets of \$7,200. Accordingly, the median home price owned by a White household was \$130,000, versus a median of



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SUMMARY OF FINDINGS

Latinos and Blacks were Steered Disproportionately into the Subprime Market...

- Latinos and African Americans received high-cost loans at a rate two to three times that of Whites.
- Among borrowers with the highest FICO scores (>720), 13.5% of Latino and 12.8% of African Americans received high-cost loans, compared to 2.6% of White borrowers with FICO scores above 720.
- 45.2% of Latino and 42.9% of African American borrowers received their loans from *independent, non-federally regulated mortgage companies*, compared to 29.2% of Whites.
- The majority of Latino and African American households whose homes were foreclosed were middle-class, earning \$60,000 to \$120,000.

...Even when Controlling for Income.

- Middle and upper income (MUI) African Americans and Latinos are actually *more* likely than lower and moderate (LMI) income African Americans and Latinos to receive subprime loans
- *MUI African Americans* were twice as likely as MUI Whites to receive a subprime loan 71.4% of the major metropolitan areas in the US
- *LMI African Americans* were twice as likely as LMI Whites to receive a subprime loan 47.3% of the major metropolitan areas in the US
- *MUI Latinos* were twice as likely as MUI Whites to receive a subprime loan 22.5% of the major metropolitan areas in the US
- *LMI Latinos* were twice as likely as LMI Whites to receive a subprime loan 4.85% of the major metropolitan areas in the US

\$92,000 for a home owned by a Latino or African American household. (Aizcorbe, et al., 2003)

As of 2006, 33% of middle-income African American households and 41% of middle-income Latino households were at risk of slipping out of the middle class, compared to 25% of the general population. (Demos, 2007)

Income is No Shield...

The vast majority of households experiencing foreclosure are middle income, earning between \$60,000 and \$120,000 annually. (Federal Reserve Bank of San Francisco, 2009) In addition, middle and upper income (MUI) African Americans and Latinos were actually more likely than lower and moderate income (LMI) African Americans and Latinos to receive subprime loans in a majority of metropolitan areas. (NCRC, 2008)

Specifically, middle- and upper-income African Americans were twice as likely as MUI Whites to receive a subprime loan in 71.4% of the major metropolitan areas in the US, and MUI Latinos were twice as likely as MUI Whites to receive a subprime loan in 22.5% of the major metropolitan areas in the US.

In contrast, low- and moderate-income African Americans were twice as likely as LMI Whites to receive a subprime loan 47.3% of the major metropolitan areas in the US, and LMI Latinos were twice as likely as LMI Whites to receive a subprime loan 4.85% of the major metropolitan areas in the US. (NCRC, 2008)

Notably, a *New York Times* analysis of mortgage lending in New York City found that “Black households making more than \$68,000 a year were nearly five times as likely to hold high-interest subprime mortgages as whites of similar or even lower incomes.” (NYT, 2009)

Did CRA Force Banks to Make Bad Loans?

The Community Reinvestment Act (CRA) rates large financial institutions based on three practices: their lending, their investments, and their services. Financial institutions must demonstrate to regulators that its activities in each of these three sectors are adequately serving the communities in which they have market presence.

Analysis of federal mortgage records shows that only 25% of the subprime mortgages that are now causing the

collapse of the credit markets were originated by CRA-regulated institutions, which include all institutions also regulated under the FDIC. The remaining 75% of subprime mortgages were originated by independent mortgage brokers or by unregulated subsidiaries of regulated banks. (Barr, 2008)

Overall, CRA-regulated banks were 66% less likely to originate high-cost loans than unregulated banks. The same holds true for low- and moderate-income borrowers; CRA-regulated banks were 58% less likely to originate high cost loans to such borrowers. (Traiger & Hinckley, 2008)

What this fact uncovers is that the subprime crisis is not a result of too much regulation, but rather the result of nonexistent regulation over the activities of independent mortgage brokers. In fact, the lack of regulation over independent mortgage companies created an uneven market, in which the independent companies undercut prices for mortgage loans, thereby stripping market share from CRA-regulated banks.

CRA-regulated banks held only 22.8% of the mortgage market in the 15 most populous metropolitan areas in the country. In addition, CRA-regulated banks held only 9.2% of the market for high-cost loans, defined as those loans where the rate spread with the Treasury yield is three percentage points or greater. (Traiger & Hinckley, 2008)

One of the most important roles of CRA is to ensure that banks are operating branches and offering services in lower-income communities. Thirty-one years forward of the passing of CRA, lower-income communities are often still banking deserts. A 2008 study done at Case Western Reserve University demonstrated that that loans originated by financial institutions without a local branch had foreclosure rates of 19.08 percent compared to only 2.43 percent for loans originated by local banks. (Fed SF, 2008)

Conclusion

The disproportionately negative effect of the foreclosure crisis on wealth in communities of color will only increase the already-existing gulf between White wealth and minority wealth, as well as lower credit scores in communities of color. These communities now face even

greater and multiple obstacles to increasing and maintaining the wealth they need to rise out of poverty.

First, and perhaps worst of all, continual tightening of credit and increased reliance on credit scores by financial institutions to obtain access to lines of credit is likely to handicap the community's ability to access wealth-building credit for many years to come, hindering a recovery here more than anywhere else.

Higher vacancy rates due to foreclosure in neighborhoods where people of color are the majority represent yet another way in which these communities are leaching wealth. Neighborhoods with high vacancy rates exhibit increased danger from looters and intruders into abandoned property and loss of neighborhood cohesion, resulting in plummeting property values. In addition, homes sold through foreclosure auctions at a considerable discount will further depress values of surrounding properties.

With the destabilizing of homeownership communities of color also comes the loss of wealth to local businesses due to fewer customers. Particularly in majority-Latino communities, over 80% of jobs within the community are created by local small businesses, and these businesses in turn draw the majority of customers from their local areas. Loss of business due to a decreased customer base has a ripple effect in terms of loss of jobs, which in turn can lead to increased foreclosures.

Hence, even as market analysts predict the end of the recession, recovery will still be a long way away for America's most vulnerable communities.

Recommendations

1. Continue to enact measures to protect homeowners who are currently in or in danger of foreclosure, including moratoria.
 2. Funnel Home Affordable Modification Program (HAMP) funds through community organizations already working in communities of color to modify failed mortgages and provide stable homeownership opportunities.
 3. Support a 30-year, government-guaranteed mortgage available for all families at 120% or below the median income, with a maximum fixed rate of 4.5%. These loans should be available only for up to the median regional home price.
 4. Ensure that the proper safeguards are in place during the home appraisal process.
 5. Develop new and creative products and marketing to serve and build trust with the unbanked, immigrants, and the poor.
 6. Provide mortgage terms in plain language to all borrowers before signing.
 7. Ensure that financial institutions uphold their fiduciary duty to borrowers with each mortgage origination.
 8. Expand CRA to all financial institutions.
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