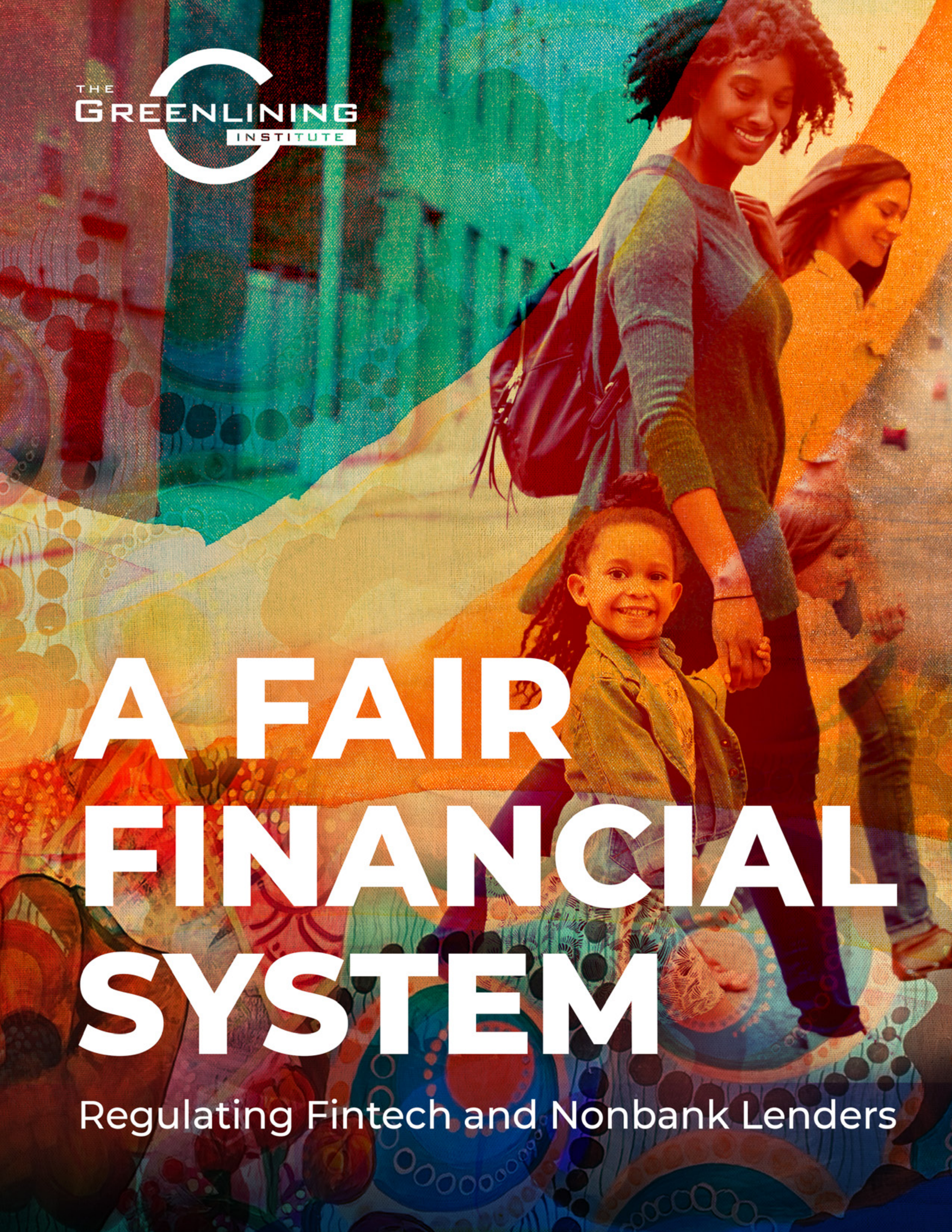

THE GREENLINING INSTITUTE

A FAIR FINANCIAL SYSTEM

Regulating Fintech and Nonbank Lenders

A FAIR FINANCIAL SYSTEM

Regulating Fintech and Nonbank Lenders

EXECUTIVE SUMMARY

Nonbank mortgage lending has grown exponentially in the last decade, to the point that most traditional banks have partnered with nonbanks to provide services and products. Nonbanks' utilization of fintech technological innovation, including algorithmic data to determine qualified borrowers, could increase economic opportunities for communities that have historically been without financial services. However, lack of data transparency—combined with the fact that these firms are subject to fewer regulations than their bank peers, with no obligations for community reinvestment—raise concerns that the rise of nonbank lenders could exacerbate inequities in low-income communities and communities of color.

Through conversations with community organizations and consumer advocates, as well as a comprehensive literature review, The Greenlining Institute developed recommendations for nonbank lenders and regulatory agencies at the state and federal levels that will embed greater equity into our financial system. These policy changes will require nonbank lenders to meet and surpass the standards held by their traditional bank peers, resulting in greater access to safe mortgages, expanded first time homeownership programs, access to entrepreneurship, affordable housing development and community-driven investments into low-and moderate income communities.

Policy Recommendations for an Equitable Financial System

Nonbank lenders can make these changes to become better community-serving institutions:

- **Maintain a race-based lens** by ensuring that safe products and services are accessible to the most underserved communities, and hiring diverse staff and leadership.
- **Build community partnerships:** Nonbank lenders should develop and strengthen relationships with community organizations in order to effectively understand the capital needs of their borrowers, create products that effectively serve the community and fund essential, local nonprofits led by people of color.
- **Prioritize culturally competent products,** especially when it comes to services and marketing. Loan underwriting, including fintech algorithms, should consider a customer's ability to repay, rather than relying on mostly the client's credit history.

State and federal lawmakers can implement these urgent policies to drive greater community investments:

- The Biden Administration should work with Congress, the Federal Reserve, the Office of the Comptroller of the Currency and the Federal Deposit Insurance Corporation to strengthen the Community Reinvestment Act and for Congress to expand the scope of the CRA to include nonbank lenders.
- California regulators should update existing California lending law to include consumer safeguards and transparency requirements to ensure equitable lending practices.
- California should build on the regulatory minimum set at the federal level and develop a state CRA similar to Illinois and Massachusetts. This would include modernization of the CRA parallel to what we propose at the federal level to include a variety of lenders and services and to expand the CRA to have a race-conscious element through a fair lending review.

Through data transparency to ensure equitable lending, increased oversight for a quickly expanding industry, and an expansion of the Community Reinvestment Act in California and federally, we can build a stronger financial system that includes nonbank mortgage lending.

INTRODUCTION

The market share of home purchase mortgage originations has steadily and substantially shifted from banking institutions to nonbank[1] lenders over recent years. In 2019, The Greenlining Institute found that five of the 10 largest home lenders in California are nonbanks,[2] and based on 2020 HMDA data, Rocket Mortgage and United Wholesale Mortgage are the biggest mortgage lenders in both the nation and California.[3] And yet, these lenders are not subject to the community reinvestment or transparency regulations that govern traditional banks. Nonbank lenders are exempt from the requirements of the Community Reinvestment Act, a federal law passed in 1977 to reverse redlining and meet the credit needs of low-to-moderate income communities. CRA is critical for obligating banks to meet the needs of LMI borrowers and, although race-blind, is an important tool for addressing the widening racial wealth gap and increasing access to first-time homeownership.[4]

TOP MORTGAGE LENDERS IN CALIFORNIA IN 2020[5]

RANKING	LENDER	TYPE OF LENDER	CA MARKET SHARE
1	Rocket Mortgage	Nonbank	11.45%
2	United Wholesale Mortgage	Nonbank	10.07%
3	LoanDepot	Nonbank	3.63%
4	Wells Fargo Bank	Bank	3.46%
5	Bank of America	Bank	2.50%
6	JPMorgan Chase Bank	Bank	2.38%
7	Freedom Mortgage Corporation	Nonbank	2.15%
8	Flagstar Bank	Bank	1.71%
9	Finance of America	Nonbank	1.67%
10	U.S. Bank	Bank	1.59%

Nonbank lenders are highlighted in green.

In recent years, nonbank mortgage lenders have originated nearly four out of five Federal Housing Administration insured loans, becoming dependent on taxpayer subsidies to maintain their business model.[6] Nonbank lenders target communities that have been historically denied access to financial products and services from traditional banks, resulting in more nonbank consumers that identify as people of color and low-to-moderate income. While Greenlining commends the leadership of nonbank lenders in leveraging new technology to create products for these populations, we have a limited understanding of the cost and impact of these mortgage products on communities of color and low-to-moderate income communities.

In this policy brief, we attempt to understand the impact of nonbank lending on communities of color and LMI communities and the problems created by leaving them largely unregulated and having no obligations for responsible lending and community reinvestment.

Expanding the CRA to nonbank lenders and insurance companies is a priority of the Biden administration[7] and the Federal Reserve in their recent rulemaking process. While that process proceeds, California can and should incentivize lenders operating in and headquartered in the state to increase lending transparency and to invest in the communities that they serve. We believe that nonbank mortgage lenders have the capacity to become better community institutions and lead with equity at the forefront.

KEY TERMS

Nonbank Lender
Nonbank lenders are financial institutions that offer typical bank-related lending services but are not deposit-taking institutions offering checking or savings accounts. Many nonbank mortgage lenders are online only, with no physical branch services. Most nonbank mortgage lenders offer consumers just two major services: home loans and loan refinancing. This policy brief is limited to nonbank mortgage lenders. Nonbank lenders fund mortgage loans by using credit — they bundle and sell the mortgages to investors or to government securities while maintaining the responsibility of collecting payment from consumers.

Fintech
Fintech refers to financial technology software and other modern technologies used by businesses that provide automated and improved financial services.[8]

Traditional Bank
For the purpose of this policy brief, a traditional bank is a financial institution that has a physical presence, like branch locations, throughout its servicing network, and also offers deposit-taking services.

Mortgage Loan
A type of loan you can use to buy or refinance a home without having all of the cash upfront.[9]

Refinance

The process of getting a new loan for your home to replace an existing mortgage. The new mortgage loan pays off the old one, leaving the borrower with just one loan and one monthly payment.[10]

Federal Housing Administration Loan

A mortgage that is insured by the Federal Housing Administration and issued by an FHA-approved lender. FHA loans are designed for low-to-moderate-income borrowers; they require a lower minimum down payment and lower credit scores than many conventional loans.[11]

Conventional Loan

The most common loan in the mortgage industry. These are funded by private financial lenders and then sold to government-sponsored enterprises like Fannie Mae and Freddie Mac.[12]

Community Reinvestment Act

The Community Reinvestment Act, enacted in 1977, requires federal banking regulators to encourage deposit-taking financial institutions to meet the credit needs of the communities in which they do business, primarily low- and moderate-income neighborhoods.[13]

Low to Moderate Income

Refers to borrowers who report an income up to 120% of the region's Area Median Income, as defined by the U.S. Department of Housing and Urban Development.[14]

POC

POC refers to people of color, including Black, Indigenous, Latino, Asian & Pacific Islander, and other non-White communities.

METHODOLOGY

This report is based on original qualitative data and a literature review.

Qualitative Data

Interviews were conducted with stakeholders between January and April 2021. The stakeholders interviewed represent consumer advocates, community-based organizations throughout California, and academia. Greenlining reached out to several nonbank lenders that were unresponsive or unwilling to speak with us on this topic, as well as to regulatory agencies that were unable to speak on this topic, so we were unable to include their perspectives.

Literature Review

Existing research was consulted before and after the interview process to provide background information and context to substantive interview findings.

GROWTH OF NONBANK LENDING

An Explosion in the Mortgage Market

Nonbank mortgage lenders grew significantly after the Great Recession, with most of their market penetration in cities hardest hit by the foreclosure crisis.[15] Nonbank mortgage lenders went from originating just 10% of mortgage originations and 6% of mortgage refinances in 2009 to accounting for nearly 66% percent of all new mortgage originations nationally as of 2020. Nonbank lenders originate more refinanced loans in the U.S. than the five largest traditional banks combined.[16] Currently, nonbank lenders dominate the mortgage lending and refinancing market, outcompeting traditional bank lenders.

How did nonbank lenders come to dominate the mortgage market?

A mix of factors combined to shift lending market share:

- Nonbank lenders invested heavily in technological growth and eased the approval process, enabling potential borrowers to receive a mortgage quote in less than 10 minutes.

- The increased regulation of traditional bank lenders following the recession evened out the playing field. A study conducted by the Federal Deposit Insurance Corporation determined that the regulatory burdens placed on traditional bank lenders account for 60% of nonbank lender growth, while technology accounted for roughly 30% of their growth.[17]
- The federal government's Financial Stability Oversight Council believes that traditional banks have shied away from mortgage lending due to the increasing legal and reputational risks that come when the housing market has a downturn, like occurred in 2008. Mass mortgage delinquencies and foreclosures leave consumers and regulators distrusting and suing banking institutions. These traditional banks make most of their profits from activities other than mortgage lending, so many have moved away from the mortgage market in recent years.[18]

So nonbank mortgage lenders are partly filling the hole left by traditional banks — they focus primarily on mortgage origination, mortgage servicing, or both. They don't have to risk the profits of other, unrelated ventures like traditional banks, can access customers online without a physical presence, and are not subject to most government banking regulations because they are not deposit exchanging institutions. These advantages don't go unnoticed by financial institutions — nearly 80% of financial institutions have entered into partnerships with fintechs and nonbank lenders in the last decade.[19]

> ***"You see activities that had once been principally the province of banks moving into the nonbank sector."[20]***
>
> **— FEDERAL RESERVE CHAIR JEROME POWELL**

An Under-Regulated, Systematic Risk

Despite the increasing number of nonbank lenders, these institutions are inherently risky. The Conference of State Bank Supervisors (CSBS) found that, in general, the largest nonbank servicers have limited liquidity, or cash on hand, due to lack of government regulations.[21] Nonbank lenders often have just enough cash held to cover a few months of operating and interest expenses — not a good sign when mortgage lenders only have one or two streams of revenue, unlike traditional banks.[22] And nonbank lenders currently have approximately four times as much debt as they do in equity — a stack of cards that can fall over at any minute.

This raises questions about nonbanks' ability to perform during a downturn in the housing or mortgage market. Nonbank lenders service nearly two-thirds of FHA loans, most of which are used by low-income, minority and first-time homebuyers, so the lack of security from nonbank lenders in case of an economic downturn will primarily harm low-and moderate income communities.[23] Should nonbank lenders be unable to extend credit, these clients could potentially experience significant changes in the availability and security of their loans.

As they say, history doesn't repeat itself — it rhymes. At a systematic level, experience shows that when a significant market downturn occurs, the failure of one major nonbank can spread to other nonbank lenders. As we learned with the Great Recession, when consumers and institutions have a lack of trust in services when a major player fails, the contagion of failure throughout the mortgage sector is possible. At a micro level, low-income communities and communities of color will again face most of the financial consequences from decisions made by the government and private sector.

NONBANK LENDERS AREN'T REGULATED LIKE THEIR BANK PEERS

Federal Regulation of Nonbank Lenders

There is currently no overarching nonbank-specific regulation at the federal level. Additionally, since most fintech or nonbank lenders operate outside the confines of banks, a sole federal regulator does not have jurisdiction over them. The Consumer Financial Protections Bureau (CFPB) has some oversight power over nonbank lenders, but their power is severely limited since Congress hasn't granted them the full legal powers needed to effectively regulate nonbank lenders.[24]

No CRA Obligations

The Community Reinvestment Act is an affirmative obligation requiring deposit-taking financial institutions to lend, invest and serve low- and moderate income communities where a bank is visible and takes deposits. Although nonbank mortgage lenders often operate like traditional banks, they are not subject to CRA investment requirements since they are not depository institutions.[25]

State Regulation of Nonbank Lenders

Under the Dodd-Frank Wall Street Reform and Consumer Protection Act of 2010, state regulators can directly enforce several aspects of federal law. States have the option to build on federal law to regulate the lending industry more closely, including oversight to restrict predatory lending.[26] In California, the Department of Financial Protection and Innovation (formerly the Department of Business Oversight) grants nonbank mortgage lenders and other fintechs a consumer lending license to lend to consumers in the state. Once licensed, the lender is required to maintain compliance with federal and state law through periodic reporting and compliance examinations.[27]

Limited Transparency Requirements

Because they are not legally required to report the race of loan applicants, a disproportionate number of nonbank mortgage applications are missing this information. This lack of transparency makes it difficult to assess potential discriminatory lending practices impacting communities of color. In addition, nonbank firms are not legally required to share algorithms with regulators, making investigating algorithmic bias in underwriting non-mortgage lending effectively impossible. Currently, few nonbanking services are required by law to collect data to ensure equitable lending, while others are prohibited from doing so.[28]

IMPACT OF NONBANK LENDING ON COMMUNITIES OF COLOR

Analysis from the National Community Reinvestment Coalition found that a greater percentage of banks made a greater percentage of loans to LMI borrowers and census tracts than non-banks and credit unions.'[29] This is largely due to Community Reinvestment Act requirements for traditional banks.

Importantly, the disproportionate amount of fintech loan applications that do not include race information make it difficult to assess the prevalence of discriminatory lending practices. UC Berkeley researchers found that lenders charge Latino and Black borrowers slightly higher rates for purchase and refinance mortgages, costing borrowers an extra $765 million annually compared to similar White borrowers. At the same time, they found that online firms discriminate 40% less than face to face loan officers in mortgage-application approvals. Evidence also suggests that at least 6% of Latino and Black applicants are rejected for mortgages that would have been accepted if the applicant was not a person of color. Black applicants are also more likely to be denied by a nonbank lender than by a traditional bank.[30]

Potentially inferior loan products and services

In the mortgage sector, LMI communities often don't qualify for conventional loans from traditional banks.This leads to nonbank lenders increasingly servicing LMI communities due to their larger offerings of FHA loans.[31] Additionally, research shows that nonbank lenders base their business models on providing FHA loans — to the point that if a customer also qualifies for a conventional loan, the fintech lender may tell the customer that they only qualify for the FHA loan option. While FHA loans are critical for meeting the credit needs of many LMI borrowers, it is not always clear that they are a borrower's only option. The lack of lending data from nonbanks makes this impossible for consumer advocates to check for. This is concerning as FHA loans often have higher monthly payments.

Decline of bank mortgage lending and CRA obligations

In the past 12 years, branch presence has significantly declined as traditional financial institutions have begun conducting more and more business online.[32] The recent pace of decline — an average of 1,467 branch closures a year — is up from an average of around 800 branch closings a year between 2008 and 2017. From 2017 to 2020, the U.S. lost about 5% of its bank branches.[33] Bank closures primarily impact low-and moderate income communities because a bank

closure in an LMI area relieves a traditional bank from it's CRA investment obligations. Since traditional banks are purposefully skirting their CRA requirements with branch closures, this creates an opportunity for fintech and nonbank lenders to offer quick and easy online financial services to meet the communities' needs for mortgages and small business loans. Consumer Financial Protection Bureau research found that an estimated 60 to 70% of loans are originated by institutions that are not covered by the federal CRA, including loans originated by credit unions and nonbank mortgage lenders.[34]

The Center for American Progress found that the exclusion of nonbank lenders from CRA requirements may leave borrowers of color exposed to issues such as steering, redlining or other predatory practices that CRA bank examinations help prevent from happening.[35]

The National Community Reinvestment Coalition argues that if one segment of the lending industry — like traditional banks— complies with CRA requirements while other segments like nonbank mortgage lenders do not, this ultimately will make lending to underserved communities more difficult.[36] The uneven regulatory landscape incentivizes traditional banks to close branch locations — resulting in a domino effect of declining CRA investments while nonbank lenders grow and fill in the space.[37]

"I would just say as a general matter, like activities should have like regulation, … consumers require protection and low- and moderate-income communities require credit support, regardless of the nature of the institution."[38]

— FEDERAL RESERVE CHAIR JEROME POWELL

The NCRC study goes farther and estimates that the current loss of 10 to 20% in loan volume to low- and moderate-income census tracts is the result of this domino effect. If current trends continue, we expect a loss of $52 billion to $105 billion in loans to low- and moderate-income census tracts nationally in the next five years.[39] That means a loss of first time home buyer assistance programs, philanthropic investments, affordable housing construction and more to LMI communities, particularly people of color.

POLICY RECOMMENDATIONS

Six Standards for Equitable Investment

Our Greenlined Economy Guidebook introduces six standards for equitable investment that are intended to address the failures of equity in our current models of investment. Without clear standards, we end up reinforcing the structures that caused problems in the first place.

For purposes of this report, we've adapted these six standards to apply specifically to the financial industry. These are the standards nonbank lenders, state regulatory agencies and federal regulatory agencies should follow when both considering their role in driving community reinvestment and when obligating institutions to do so.

1. **Emphasize Anti-Racist Solutions:** Race-conscious policies like redlining and urban renewal got us to this point, and race-neutral approaches can't fix the underlying inequities. Investment needs to target and prioritize the most impacted communities.
2. **Prioritize Multi-Sector Approaches:** Policies and institutions may be siloed, but problems are not. Financial institutions need to prioritize approaches that address multiple issues and barriers at once.
3. **Deliver Intentional Benefits:** Benefits cannot trickle down to communities; they need to go directly to the people in the most impactful ways, while avoiding increasing or creating new burdens.
4. **Build Community Capacity:** Long-term disinvestment and discriminatory policies can erode a community's capacity for leadership. Focusing on capacity building of leaders of color in financial institutions and supporting nonprofits led by people of color is a key part of improving investments.
5. **Be Community-Driven at Every Stage:** Community members and organizations should be part of every phase of investment and services, from development to implementation.
6. **Establish Paths Toward Wealth-Building:** We need community ownership of assets and opportunities to continue building wealth, with lower barriers to entry.

Equity in financial services necessitates broad systems change and understanding of the responsibilities that financial institutions have in meeting the needs of the communities they profit from. Banks and nonbank lenders alike can and should correct the legacy of redlining by reinvesting the wealth they receive from consumers and the subsidies they receive from the government.

Despite the known barriers to comprehensive systems change right now, the following policy recommendations aim to move financial institutions toward achieving these community investment standards in order to build an equitable and inclusive financial system.

Policy Recommendations for Nonbank Lenders

Nonbank lenders should be held to the same standards that Greenlining and other advocates hold traditional bank mortgage lenders to. Through our conversations with community based organizations, we identified several ways that nonbank mortgage lenders can be better community institutions.

Maintain a race-based lens:

Nonbank lenders must meet the credit needs of borrowers and neighborhoods of color in order to redress the harm financial institutions have caused communities of color through historical redlining and continued predatory lending and discriminatory practices. Nonbank lenders can keep race at the forefront by considering the impact of their marketing and lending on specific communities, actively working to make safe products and services accessible to the most underserved communities, and hiring diverse staff and leadership.

Build community partnerships:

While nonbank lenders operate largely online, they still can serve a particular community. Many of the organizations we spoke to noted that they do not have any relationships with nonbank lenders, despite the number of loans that nonbank lenders make in their communities. Nonbank lenders need to develop and strengthen relationships with community organizations in order to effectively understand the capital needs of their borrowers, create products that effectively serve the community and fund essential, local nonprofits led by people of color.

Strong community partnerships allow nonbank lenders to lean on community organizations to provide critical services to borrowers, such as first-time homebuyer education programs and support in developing grant programs for first-time home buyers. These critical services both reduce risk for the lender and expand access to homeownership for low-income communities and communities of color.

Culturally competent products, services and marketing:

Nonbank lenders should increase cultural competence in both products and affirmative marketing to communities of color. Loan products and underwriting should be accessible to communities that have been historically denied access to credit or have been negatively impacted by predatory lending. As such, underwriting should consider ability to repay, rather than simply relying on credit history.

Lenders should invest heavily in ethnic media for their marketing efforts, which will help them both ensure that they reach consumers not well served by mainstream media as well as help to support businesses owned by people of color. Further, lenders should prioritize delivering their products and services in the languages spoken by California's diverse communities and ensure that all communities, regardless of English proficiency, are protected against predatory practices and treated fairly.

Proposed Policy Timeline

While nonbank lenders have an opportunity to lead as community institutions, state and federal regulatory agencies must take legislative action to require greater transparency, regulation and community reinvestment. This is an urgent issue and we propose the following policy development phases to move toward greater community reinvestment obligations at the state and federal level.

CA/FEDERAL	PHASE	POLICY
CA	1	Update existing California lending regulation to include CRA-type consumer safeguards and data transparency requirements
CA	2	Create a state CRA for credit unions, nonbank mortgage lenders and insurance companies
Federal	3	Expand the Community Reinvestment Act to include nonbank lenders, insurance companies and credit unions; apply a race lens in order to specifically address the impact of redlining

Policy Recommendations for California

Our communities can't wait on federal regulators to catch up to the 21st century and to modernize the Community Reinvestment Act. The state of California has the power to advance the priorities of equitable and inclusive mortgage lending and should act independently.

Timeline: Our proposed timeline for state regulatory change takes into consideration the lack of information on the nonbank lending industry at the state level. The recommendations are divided into two phases: 1) updating state lending regulations to include fair lending safeguards and ultimately, 2) the creation of a state level Community Reinvestment Act.

Update existing state lending regulation to include fair lending safeguards:

Increase Transparency Requirements

Before California institutes a state-level CRA, we must increase transparency requirements for nonbank lenders in order to accurately understand the impact nonbank lending has on LMI communities and the industry's practices around equitable lending. Currently, advocates and regulators lack sufficient local data and research on the lending practices of nonbank lenders. The lack of data transparency complicates regulation, since data-driven evidence of serious consumer infractions and examples of systematic discrimination are needed for regulators to take action.

Nonbank lenders are able to avoid federally mandated examinations, but since nonbanks are subject to state regulations to receive lending licenses, the Department of Financial Protection and Innovation can request additional information to grant lending licenses annually.

Empower the DFPI to Evaluate Fair Lending

The DFPI should be expanded to request data transparency and fill the information gap left by federal regulators for nonbank lenders. Under its authority to request additional information from licensed lenders in the state, the DFPI should require licensees to provide data needed to conduct a fair lending test similar to the one conducted by federal regulators for traditional banks under the CRA. This small change in enforcement will ensure equitable consumer safeguards for all California consumers purchasing loans from nonbanks. In addition, the increased examination would disincentivize fintech firms from failing to comply with fair lending standards and help root out bad actors and their practices. If nonbank lenders are following the rules, they shouldn't worry about state regulators checking and ensuring that their loans are equitable — they would be held to the same level of accountability as traditional lenders.

Create a California Community Reinvestment Act:

Unlike traditional banks, nonbank lenders are not covered by the federal Community Reinvestment Act, despite the similarity in their products and services. As such, nonbank lenders should have the same mandate to serve LMI communities as traditional bank lenders and this mandate can come from the state.

Precedent for State CRAs

California would not be the first state in the nation to create a state CRA. Four states — New York, Connecticut, Illinois and Massachusetts — have implemented a CRA to meet the needs of their community.[40] Here, we look to Illinois and Massachusetts as examples of how a state CRA can be implemented in California.

> ***"The Illinois CRA will complement the federal Community Reinvestment Act, a state CRA enables Illinois to help direct state-chartered financial institutions' lending, services, and investments to promote state-specific priorities, such as efforts to prevent displacement and enable lower income residents in gentrifying areas to be able to remain in affordable housing in their neighborhoods."[41]***
>
> **— EXECUTIVE DIRECTOR OF THE WOODSTOCK INSTITUTE HORACIO MENDEZ**

Illinois Community Revitalization Act

In March 2021, Illinois enacted the Illinois Community Revitalization Act that includes state-chartered banks, state-chartered credit unions and nonbank mortgage lenders. The state reinvestment act is designed to incentivize additional safe lending practices toward low-income and moderate-income communities. The Illinois Department of Financial and Professional Regulation, similar to California's DFPI, is responsible for developing rules and procedures for the evaluation and oversight process, which must include a public participation component.[42] The department also conducts the CRA examinations of major lenders within the state.

Massachusetts Community Reinvestment Act

The Massachusetts CRA has applied to state-chartered credit unions, state-chartered banks and nonbank mortgage lenders since the early 1980s, and there have been no observable negative consequences. Rather, the state CRA in Massachusetts is directly responsible for expanding home ownership opportunities for people of color and lower income people.

Massachusetts CRA exams for mortgage companies and banks are more rigorous than the federal standard, particularly in fair lending reviews and examinations for abusive lending. The Massachusetts lending tests include a section called "loss of affordable housing" that investigates whether abusive lending, shown in high delinquency and default rates, has caused LMI borrowers to lose affordable housing stock.[43] In addition, the Massachusetts CRA includes a racial equity lens, in which their state-administered fair lending review compares a mortgage company's percentage of applications from racial and ethnic groups to peer lenders.[44] For racial justice advocates, the Massachusetts' community reinvestment model is the gold standard nationally.

Based on these examples, a state-level CRA in California can do the following:

- Incentivize relationships between nonbank lenders and nonprofit organizations that serve LMI communities and communities of color.
- Rebuild and significantly increase investments in low-to-moderate income communities that do not have access to physical banks in their communities.
- Require that the best possible mortgage products are offered to clients.
- Ensure corporate accountability for financial institutions.
- Test for fair lending to all racial and ethnic groups, in comparison to peer lenders.

In addition, a California CRA should require credit unions, mortgage lenders and insurance providers to also be regulated to invest in low-to-middle income communities. The California CRA should also be a mechanism for expanding beyond the limitations of the federal CRA — requiring that traditional banks without a physical presence in low-to-middle income communities to still invest in these areas. A major benefit of creating a California CRA would be adopting features similar to the Massachusetts model, creating a racial equity lens in examining lending practices to ensure that communities of color are treated equally with White community members.

Policy Recommendations for Congress and Federal Regulatory Agencies

Expand the Community Reinvestment Act:

The federal Community Reinvestment Act remains critical for driving traditional bank lending in low-to-moderate income communities. The Penn Institute for Urban Research confirmed that despite the increase in home lending by non-bank and online lenders relative to traditional banks, CRA is what has made sure banks continue to lend to LMI communities.[45] Congress expanding CRA requirements to cover nonbank lenders would help enforce responsible lending from all lenders (thereby lowering the chance of delinquency and default across the market), as well as encourage lenders to compete in delivering safe and sound products. In addition to traditional banks, nonbank lenders, including non-depository mortgage companies, fintech and online lenders, and credit unions, should be assessed in their lending based on where they make loans, and should have an obligation to reinvest locally.

Apply a Race Lens

Banks and nonbank lenders should be evaluated based on their lending, services and investments in neighborhoods of color and to borrowers of color, in order to ensure that CRA activity addresses the impact of redlining. Financial institutions should be unable to pass their CRA examinations if a regulator finds evidence of discrimination based on race or ethnicity.

For the CRA to continue to be effective at obligating banks to lend responsibly to communities of color, it must include the nonbank lenders that are increasingly becoming a large part of the financial landscape.

We urge the Biden Administration to work with the Federal Reserve, the Office of the Comptroller of the Currency, and the Federal Deposit Insurance Corporation to strengthen the Community Reinvestment Act and Congress to expand the scope of CRA oversight to include nonbank lenders. Strengthening the CRA is a critical step to addressing the nation's racial inequities.

CONCLUSION

Nonbank lending represents an opportunity to finally serve the low- and moderate-income communities that have historically been excluded by traditional banks, despite gains made because of the CRA. This is also an opportunity for nonbank lenders and regulators to ensure they do not take the route of payday lenders — taking advantage of people in precarious situations to increase profit margins.

Historically, unregulated growth results in economically disastrous outcomes, which primarily impacts low-and moderate-income communities and communities of color. Nonbank lenders must show leadership to better serve the communities that they are now a part of and to be transparent about their lending practices. At the same time, the state and federal governments must update existing laws to ensure that the same regulatory standards are applied to all industry players — this includes legally ensuring equitable lending practices and community investment standards.

If the current trend continues, disparate lending will result in money disproportionately leaving the pockets of Black and Latino consumers while fewer investments are being made in the communities that they live in. Based on a variety of factors discussed in this paper, it is expected that in the next decade, billions of dollars will be extracted from LMI communities, but the timeline set in this paper can reverse that trend. Even better, we expect that a California CRA will result in *greater* investments in these communities, resulting in billions being invested in these communities rather than extracted from them. In addition, if the state could possibly legally harness nonbanks' alternative lending algorithms, we could expand these methods to accept more qualified people for mortgage loans that would otherwise be denied loans from traditional banks.

A California CRA and a modernized federal CRA will help significantly close the racial wealth gap, create intergenerational wealth, build more affordable housing, increase first-time homeownership, and so much more. We, as a society, just have to finally do what is right — to stop extracting wealth from the most vulnerable and to instead, start investing money to help the communities that were and still are subject to systematic economic disinvestment.

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ABOUT

The Greenlining Institute

The Greenlining Institute works toward a future when communities of color can build wealth, live in healthy places filled with economic opportunity, and are ready to meet the challenges posed by climate change. To achieve this vision, Greenlining is committed to building a just economy that is inclusive, cooperative, sustainable, participatory, fair and healthy. Our multifaceted advocacy efforts address the root causes of racial, economic and environmental inequities in order to meaningfully transform the material conditions of communities of color in California and across the nation. We act as an incubator of new policy ideas, a bridge builder between people, communities and government, and an advocate to build momentum for transformative change.

Authors

Muhammad Alameldin
Economic Equity Fellow

Muhammad T. Alameldin grew up in Stockton, California. Witnessing ground-zero of the 2008 foreclosure crisis, Muhammad watched one in 20 families around him lose their homes due to high-cost loans that primarily targeted people of color. Now, those same people are priced out by the housing crisis or are impacted by high rents and unfair banking practices. Muhammad got his start as a paid policy research intern for Mayor Michael Tubbs' office — where he witnessed Stockton's revolutionary Guaranteed Income pilot provide economic security for families in his hometown. Then, Muhammad moved to Washington D.C. to assist a newly founded organization, Pay Our Interns. During his time there, he successfully collaborated with Congress to establish a $17+ million annual paid internship fund on Capitol Hill. Before joining Greenlining, Muhammad was the Digital Strategist for California YIMBY, where he increased volunteer engagement so California could establish a statewide rental cap and no-hassle accessory dwelling unit construction. Muhammad's goal is to democratize access to government and economic opportunity so that anyone can achieve economic mobility without excessive hardships. His current focus is on helping solve California's housing crisis. Muhammad achieved his B.A. from the University of California Berkeley in 2019.

Rawan Elhalaby
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Rawan leads the organization's research efforts around bank accountability and financial inclusion. She is passionate about advancing equity for underserved communities through policy research, data analysis and advocacy. As the daughter of Palestinian, working class refugees, Rawan is all too familiar with the obstacles that low-income and immigrant families face in achieving self-sufficiency in the United States. She has spent her career fighting barriers to economic opportunity: at the systems level at Greenlining, and at the individual level with refugees from Iraq, Somalia, Syria and Afghanistan at the International Rescue Committee in San Diego. She has also worked as a policy consultant to the Consumer Financial Protection Bureau, the County of San Diego, the Western Regional Advocacy Project and the Dellums Institute for Social Justice. Rawan holds a Master of Public Policy from UC Berkeley's Goldman School of Public Policy and a B.A. in Political Science from San Diego State University. Rawan authored Greenlining's recent report Home Lending to Communities of Color, testified before the House Financial Services Committee's Subcommittee on Diversity and Inclusion on the lack of diversity in banks, and has been quoted in a variety of publications ranging from American Banker to Politico.

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ENDNOTES

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