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AN ANALYSIS OF THE EFFECTIVENESS OF THE HOME MORTGAGE DISCLOSURE ACT OF 1975

The Home Mortgage Disclosure Act was intended to provide information concerning "redlining." Through interviews and questionnaires the authors investigated the efficacy of the Act in Cuyahoga County, Ohio, which contains Cleveland and its adjacent suburbs. The authors conclude that local housing organizations and financial institutions find the disclosure information useful; they suggest that the Act be renewed and amended to require disclosure of information indicating demand for mortgage loans and to provide for centralized data collection and processing.

URBAN DISINVESTMENT is a topic of great, current concern in the United States. Many authors have written recently on residential lending processes,¹ "redlining,"² and the Home Mortgage Disclosure Act of 1975 (HMDA),³ as they affect disinvestment, primarily in our urban centers. Nevertheless, the existence of redlining has rarely been proved, due to the scarcity of data on the lending practices of financial institutions. Because of the mystery surrounding redlining—some claiming that it is a vital contributor to the difficulties of our cities, and others denying its existence or relevance—Congress passed the HMDA so that, "by providing facts, [it could] bring to an end more than a decade of 'red-lining' charges and countercharges."⁴

The purpose of this Note is to analyze the effectiveness of the

1. See, e.g., U.S. COMMISSION ON CIVIL RIGHTS, *MORTGAGE MONEY: WHO GETS IT? A CASE STUDY IN MORTGAGE LENDING DISCRIMINATION IN HARTFORD, CONNECTICUT* (1974); Earthman, *Residential Mortgage Lending: Charting a Course Through the Regulatory Maze*, 29 VAND. L. REV. 957 (1976).

2. See, e.g., Duncan, Hood, & Neet, *Redlining Practices, Racial Resegregation, and Urban Decay: Neighborhood Housing Services as a Viable Alternative*, 7 URB. LAW. 510 (1975); Renne, *Eliminating Redlining by Judicial Action: Are Erasers Available?*, 29 VAND. L. REV. 987 (1976); Note, *Attacking the Urban Redlining Problem*, 56 B.U. L. REV. 989 (1976); Note, *Urban Housing Finance and the Redlining Controversy*, 25 CLEV. ST. L. REV. 110 (1976). For a wide spectrum of views about redlining, see *Hearings on S. 1281 Before the Senate Comm. on Banking, Housing and Urban Affairs*, 94th Cong., 1st Sess. (1975) [hereinafter cited as *Hearings*]. These sources generally define redlining as the denial by financial institutions of mortgage loans in particular geographic areas, without regard to the borrower's creditworthiness or the property's condition.

3. 12 U.S.C. §§ 2801-2809 (1976); see, e.g., Comment, *Red-lining and the Home Mortgage Disclosure Act of 1975: A Decisive Step Toward Private Urban Redevelopment*, 25 EMORY L.J. 667 (1976).

4. H.R. REP. NO. 561, 94th Cong., 1st Sess. 4., reprinted in [1975] U.S. CODE CONG. & AD. NEWS 2303, 2306.

HMDA in meeting its stated purposes,⁵ as they relate to redlining and the residential lending process. The following analysis is based not only on information digested from literature on the subject, but also on information gathered from interviews, conducted during the first eight months of 1977, with representatives of local community and housing organizations, officers of federally regulated financial institutions, and a sample of residents of the area.⁶ All interviews reported in this Note were conducted in Cuyahoga County, Ohio, which contains Cleveland and its adjacent suburbs. Twenty-nine of the thirty-eight financial institutions in Cuyahoga County which reported for the HMDA agreed to permit interviews with a representative of their institution—generally either the chief executive officer or an officer with primary responsibility for residential mortgages.⁷ Eight of the institutions surveyed were commercial banks and twenty-one were savings and loan associations.⁸ In addition, fifteen nongovernmental organizations that

5. These stated purposes are:

to provide the citizens and public officials of the United States with sufficient information to enable them to determine whether depository institutions are fulfilling their obligations to serve the housing needs of the communities and neighborhoods in which they are located and to assist public officials in their determination of the distribution of public sector investments in a manner designed to improve the private investment environment.

12 U.S.C. § 2801(b) (1976).

6. These interviews were conducted as part of research project number 77-10655, funded by the Law and Social Sciences Program, Division of Social Sciences, National Science Foundation, Washington, D.C. The conclusions of the researchers do not necessarily reflect the opinions of the National Science Foundation.

7. Interviews were conducted with assurances of confidentiality; therefore, no housing organization or financial institution is specifically mentioned without its prior approval. Data collected during the research project is compiled in a file available upon request at the library of the Case Western Reserve University School of Law. The interviews were based on a combination of both open-ended and closed questions which were pretested with individuals not included in the study.

8. Eight financial institutions identified as active in Cuyahoga County were not interviewed. One of these, a savings and loan association, had recently completed a merger with another association which was interviewed. One major commercial bank, which was at that time the subject of much controversy over a tax abatement granted by the City of Cleveland, refused to be interviewed about bank policy. One of its assistant vice-presidents explained to the interviewers that it was bad publicity to talk about disclosure of the institution's lending policies. In contrast, a second small commercial bank declined to be interviewed because it had not made any home mortgages in ten years and had no strong feelings about the HMDA.

One savings and loan, the largest home mortgage lender among savings and loans in the county, refused to be interviewed on the ground that the National Savings and Loan League had presented their view in its report on the HMDA. One of the smaller savings and loans was not interviewed because its president was fed up with government paperwork. He had testified before Congress about the HMDA and felt there was no

work in the area of redlining and know about the HMDA were identified.⁹ Officials of each of these organizations were interviewed. Finally, eight hundred county residents were asked about their knowledge and use of the HMDA and about their relationship to housing organizations. This multistage cluster sample was representative of 1970 census data on race, sex, and age.¹⁰ The interviews were conducted to learn whether the Act has been utilized as Congress anticipated, whether it has fulfilled its purposes, and what legislative and other systemic changes are recommended to meet the problems associated with redlining.

Preceding the analysis of the Act itself, the first section of the Note provides an overview of the residential lending process, followed by a discussion of redlining. The next section describes the HMDA, its purposes and its substantive provisions, and analyzes how it is being used in Cuyahoga County. The Note concludes by considering the recommended changes in the Act and in the present system of residential mortgage lending.

I. BACKGROUND: RESIDENTIAL LENDING

Providing a "decent home and a suitable living environment"¹¹ for all has been federal policy since the Housing Act of

demand for the disclosure information. Three of the smallest savings and loans were not interviewed because each repeatedly postponed the scheduled times.

9. These organizations included countywide organizations as well as neighborhood-based groups which primarily derive their support from and center their activities in particular circumscribed areas of the county. Of the eleven with limited geographic foci, two were based in individual, inner ring suburbs of Cleveland, while the remaining nine were active in specific sections of Cleveland. More than half of the organizations ranked housing as their first organizational concern, with the types of housing concerns varying considerably. About one-third of the 15 groups focused on planning, research, and monitoring various aspects of the home delivery system. These groups, which tended to have a countywide orientation, also provided assistance to traditional neighborhood-based organizations. The latter were primarily concerned with the immediate problem of physical deterioration of the neighborhood housing stock. Their activities generally included programs for repairs, financing, and preventing abandonment.

Forty percent of the groups interviewed rely to some extent on foundation grants for their financial support. One-third receive support from church organizations. Other sources of income for these housing groups include fundraising drives, individual contributions, fees for services, contracts with local governments, and funding from government agencies. The median total budget for these community groups was \$70,000 per year.

10. Staruch, *Sampling and Sample Characteristics—Cleveland Area Survey: 1976 and 1977 (1977)* (unpublished: available at Cleveland Area Survey, Department of Sociology, Case Western Reserve University).

11. 42 U.S.C. § 1441 (1970).

1949.¹² In the Fair Housing Act of 1968¹³ Congress enacted a law "to provide, within constitutional limitations, for fair housing throughout the United States."¹⁴ One popular way for individuals to acquire housing is by purchasing homes.¹⁵ Because the cost of buying a home is more than the vast majority of Americans can afford to pay outright, the process of financing a home purchase is a vital step toward owning a home. By controlling the process of financing, a small number of persons and institutions greatly influence where, and on what terms, an individual eventually buys a home. The means of control are often so subtle that home buyers may not even be aware that the choice of where they will live is being determined directly and indirectly on the basis of factors other than their expressed needs and preferences and the compromises necessitated by the limits of their financial ability. Nevertheless, when these decisions consistently distinguish between groups of people on the basis of racial, cultural, or other noneconomic criteria, the impact on selected geographic areas that are thereby excluded from residential lending, except on noncompetitive terms, can be crippling. The effect on individuals about whom these biased assumptions are made can be exclusionary. The consistent refusal of lenders to provide residential mortgages in specific areas is commonly known as redlining.¹⁶ An overview of the process of procuring a home is essential background for analysis of the claims and counterclaims concerning redlining and for evaluating the effectiveness of the HMDA.

A. *Overview of the Home Buying Process*

The ultimate goal of the home buying process is the purchase of a house that meets the needs of the potential buyer, within the constraints of what the buyer can afford to pay. At several critical points in the process the decisions of people other than the buyer greatly influence where the individual will ultimately buy. The seller decides whether to list with a real estate broker, which broker to deal with, and on what terms. The broker decides

12. *Id.* The policy was expressly reaffirmed in the Housing and Urban Development Act of 1968, 42 U.S.C. § 1441a (1970) (amended 1974).

13. 42 U.S.C. §§ 3601-3631 (1970 & Supp. V 1975).

14. *Id.* § 3601.

15. "Almost two-thirds of all American families own their own homes." *Lending Discrimination? Look at the Facts*, 97 SAVINGS & LOAN NEWS 60 (Aug. 1976).

16. For a more detailed definition of redlining, see notes 67-72 *infra* and accompanying text.

which houses to show a particular buyer and perhaps recommends a lending institution to provide financing. An appraiser determines the value of the house, depending on various structural and neighborhood characteristics. A loan officer decides whether or not to lend, and on what terms to lend, based in part on his perceptions of the applicant-buyer's financial capacity and on the appraisal. The loan committee and officers of the financial institution set the policies on lending and review the loan officer's lending recommendations.

If the plans of a prospective buyer are frustrated by any of these decisions, the individual may be forced to find alternate sources of funds or alternate places to live. Since the actions of those involved in the home buying process can seriously impede attempts to find a suitable home and can result in loss of investment in entire neighborhoods, it is important to identify and examine the bases upon which all individuals in the chain make decisions. Of particular importance is the degree of discretion and objectivity involved at each step in the process, and the impact that each decision can have when it concurs with other decisions in the process. As decisions build on other decisions, the impact on the applicant-buyer and on various neighborhoods may be amplified, particularly if each decision tends to reinforce the other decisions in the process. These individual private decisions trigger public concern when they become more or less consistent responses that have predictably disparate effects on identifiable groups of individuals and communities.

The following description of the normative process of home buying, with particular emphasis on the financing mechanism, will illustrate the impact that individual decisions can have on a community. The emphasis on individual decisionmaking is important because it indicates how individuals who comprise part of a larger process may make decisions that result in institutional discrimination without any individual actually intending to cause the end result. The process described is one of the most common ways of buying a house. Obviously, other processes affect the total result in an area and on individuals. Moreover, the description is incomplete because information available under the HMDA only covered the regulated financial institutions; information on unregulated sources of funds, such as individuals or mortgage bankers, is not readily obtainable. Nevertheless, this description accurately characterizes the majority of residential

lending transactions which comprise an important class of transactions greatly affecting home buying and financing in this country. Nonconventional sources of home financing become important only when conventional credit is unavailable. Since nonconventional sources provide funds at higher costs than conventional sources, when the conventional lending process results in a disproportionate impact on particular areas, the effects of the private decisions within that process assume public importance.

B. *Home Financing Alternatives*

1. *Prefinancing Decisions*

The seller makes several decisions that affect the potential buyer and the neighborhood where the marketed house is located. The most important of these decisions are whether to engage a real estate broker and at what price to sell the property. If the seller contracts with a broker, the broker will show the property to some potential buyers, but not to others. As one commentator has noted: "The real estate broker has traditionally performed a 'gatekeeping' function, directing white buyers to predominantly white areas and minority buyers to minority or interracial areas."¹⁷ In addition, a decision whether or not to sell through a real estate broker will affect whether or not the ultimate transaction (or refusal to agree to a transaction) will be open to scrutiny under the Fair Housing Act of 1968.¹⁸ The practice of racial steering probably violates this Act, as does steering on the basis of sex, religion, or ethnicity;¹⁹ nevertheless, there is little question that race continues to be a consideration in many real estate practices.²⁰

The seller will also decide at what price to list and to sell the property. This price will, of course, limit the class of potential buyers to those who can afford to buy the house. Potential buyers who would otherwise be capable of buying a house in the com-

17. Note, *Racial Steering: The Real Estate Broker and Title VIII*, 85 YALE L.J. 808, 809 (1976). See also Brown, *Access to Housing: The Role of the Real Estate Industry*, 48 ECON. GEOGRAPHY 66 (1972).

18. 42 U.S.C. §§ 3601-3631 (1970 & Supp. V 1975). This Act is also referred to as Title VIII of the Civil Rights Act of 1968.

19. See Note, *supra* note 17. The author argues that Title VIII of the Civil Rights Act of 1968, 42 U.S.C. §§ 3601-3631 (1970 & Supp. V 1975), forbids real estate brokers from providing different treatment to customers on the basis of race and thus prohibits virtually all racial steering practices.

20. See, e.g., Holden, *Euclid Park Area Invasion Target?*, The Sunday Plain Dealer (Cleveland), Feb. 19, 1978, § 1, at 1, col. 5.

munity may be prevented from doing so if the seller sets a price that is higher than that for which comparable houses have been sold in the area. An extra-large down payment would be necessary to cover the amount by which the sale price exceeds the appraised value of the property.²¹ The appraised value of a house, in turn, is greatly influenced by the selling prices of comparable houses in the neighborhood.²²

The buyer must provide the seller with the monetary consideration before a house can be sold. Since most buyers do not have the money immediately available, they must arrange for financing. The successful buyer must survive a series of screening decisions²³ before acquiring the financing from one of a variety of financial institutions.²⁴ The following sections describe the alternative sources of borrowed capital and the implications of the various alternatives for both the individual borrower and the area surrounding the house being sold.²⁵

2. *Lending Institutions*

Savings and loan associations, mutual savings banks, and commercial banks are probably the primary sources of home financing.²⁶ In 1967, savings and loan associations were investing 90.3% of their savings capital in home mortgages, mutual savings banks had 67.5% of their total deposits invested in housing mortgages, and commercial banks had invested 20.6% of their total

21. Lenders lend no more than a certain percentage of the appraised value of the property, and no more than another higher percentage without additional security, such as FHA or private mortgage insurance. See *Hearings, supra* note 2, at 559.

22. See text accompanying notes 57 & 58 *infra*. Similarly, the price at which the seller eventually sells may ultimately affect the value of other houses in the neighborhood through the same appraisal process.

23. See notes 42-66 *infra* and accompanying text.

24. See notes 26-33 *infra* and accompanying text. The mortgage may be conventional or government insured. See notes 34-41 *infra* and accompanying text.

25. While the emphasis throughout this Note is on financing the purchase of a home, financing home repairs is another important aspect of the redlining issue. The process of obtaining a second mortgage loan for repairs or home improvements is similar to that described below.

26. For the purposes of this discussion, the differences between the various banks and savings institutions are not particularly important. Their common characteristic is that they are "depository institutions" to which the HMDA reporting requirements apply, 12 U.S.C. § 2802(2) (1976); that is, they invest deposits from customers, in addition to making loans. 12 C.F.R. § 203.2(c) (1977). On the other hand, mortgage bankers, which are in the business of just making loans, do not get their loan capital from deposits. Because they are not federally regulated, information is not available to determine accurately the role of mortgage bankers in the home mortgage market.

time deposits in housing mortgages.²⁷ These figures indicate the importance of home mortgages in the financial structure of the various institutions.

The institutions, in turn, are vital to the home buying market. In actual numbers of mortgages held in 1972, savings and loan associations had by far the greatest (188,884,000), as compared to commercial banks (90,114,000), and mutual savings banks (64,333,000).²⁸ At the end of 1973, savings and loan associations held 48.4% of all loans on one to four family houses held by the private sector in the United States.²⁹

It is apparent from this information that savings and loan associations are the most important source of residential mortgage money. Federal savings and loan associations were created by the Home Owners' Loan Act of 1933³⁰ "to provide local thrift institutions in which people may invest their funds and . . . to provide for the financing of homes . . ."³¹ Interviews in Cuyahoga County indicate that savings and loan associations continue to see themselves as savings institutions and residential mortgage lending institutions. The majority of savings and loan association representatives interviewed indicated that developing savings deposits was more important than mortgage lending for their institution. Others indicated that developing savings deposits and providing residential mortgages were given equal weight, while still others said that residential lending was their most important activity.³²

3. *Conventional and Government-Insured Mortgages*

Home mortgages are typically purchase money mortgages where the lender secures the debt by making the property purchased the collateral for the loan. The lender provides a per-

27. Renne, *supra* note 2, at 993 nn.29-31.

28. *Id.*

29. Note, *Redlining—The Fight Against Discrimination in Mortgage Lending*, 6 LOY. CHI. L.J. 71 n.2 (1975).

30. 12 U.S.C. § 1461 (1976).

31. 12 U.S.C. § 1464(a) (1976).

32. In contrast, when the commercial banks interviewed were asked the same question: "Please rank, from most important to least important, your institution's activities," none considered residential mortgage lending to be one of their most important activities. Commercial loans and consumer installment loans were their primary activities. L. McKinney & P. Pap, Financial Institutions Interview Form at 3, No. 14 (1977) (unpublished questionnaire on file in Case Western Reserve University School of Law Library) [hereinafter cited as Financial Interview].

centage of the appraised value of the property, and the borrower pays the remainder of the sale price to the bank in the form of a downpayment. The percentage of the sale price of the house that a financial institution will lend is based on what the institution believes it can recover if it should have to foreclose and sell the house; it must recoup from the sale the administrative and legal costs involved as well as the amount of money lent. Lending institutions regulated by the federal government provide conventional mortgages.³³ Nonconventional mortgages can take a variety of forms.³⁴ They are resorted to by buyers who want to buy a particular house in a particular area and have not found conventional financing. The cost of nonconventional borrowing is higher and has more onerous terms than conventional financing.³⁵

Even financing by the Federal Housing Administration (FHA), a common, nonconventional mortgage source, may be more costly than conventional financing, despite its avowed statutory purpose to make home ownership available to many people who would otherwise be unable to afford it.³⁶ The FHA has established less stringent underwriting requirements for applicants than those generally used by lending institutions.³⁷ In addition, lower interest rates and minimal downpayments offer more liberal terms for borrowing. Loans insured by the FHA provide lenders with the opportunity to make loans that are risk-free to the institution. If the borrower defaults, the lender recovers the entire unpaid principal and interest as well as foreclosure costs.³⁸

Unfortunately, abuse in the administration of the FHA program³⁹ has made FHA lending a threat to neighborhoods attempting to avoid deterioration. Speculators can use FHA property to recover a profit, foreclose quickly, and accelerate the deterioration of properties.⁴⁰ One-third of the financial institutions inter-

33. These mortgages must be reported under the HMDA. 12 C.F.R. § 203.2(d) provides the definition of federally related mortgage loans that must be reported.

34. For a discussion of nonconventional mortgage loans, see Note, *Attacking the Urban Redlining Problem*, 56 B.U. L. REV. 989, 999-1005 (1976).

35. *Hearings, supra* note 2, at 558-61 (research paper by Sternlieb, Burchell, & Listokin).

36. Note, *supra* note 34, at 1002.

37. Note, *supra* note 34, at 1001; see 24 C.F.R. § 203.43a (1977).

38. Note, *Exploiting the Home-Buying Poor: A Case Study of Abuse of the National Housing Act*, 17 St. Louis L.J. 525, 543 (1973).

39. See Note, *supra* note 34, at 1003-05.

40. Lenders make a profit by charging borrowers "points" in addition to regular FHA costs. See note 71 *infra*. Foreclosure occurs quickly because the lender can recover the full

viewed which make FHA loans indicated that they or others currently used government insured, as opposed to conventional, mortgages, when uneasy about granting loans in a particular area felt to be risky or going downhill.⁴¹ Such selectivity in lending may contribute to the problems associated with redlining and disinvestment.

C. *Institutional Lending Decisions—Practice, Policy, and Impact*⁴²

1. *The Real Estate Broker*

As indicated above, potential buyers often find the houses they want to buy through real estate brokers, who direct them to homes that, in the view of the brokers, are suitable for the buyers and in the best interests of the sellers, the brokers' clients. Brokers also play an important role in determining the financial institution that will provide the necessary funding and the terms of that funding. They are the first level in the three-stage process of financial screening that the typical buyer must undergo to acquire conventional financing from a governmentally regulated lending institution.⁴³

Savings and loan associations in Cuyahoga County indicated that they receive a substantial majority of their home mortgage applicants by referral from real estate agents.⁴⁴ In fact, the most

amount insured and its expenses from the government, and because there is no incentive to forbear from foreclosure as soon as the buyer has defaulted in mortgage payments. The buyer is then evicted, pending foreclosure, leaving the property vacant and a vulnerable target for vandals.

41. The question asked was: "Would you please react to the following sentence? When a financial institution is unsure about granting mortgage loans in a particular area, it would most likely grant only government-insured loans because such loans are risk-free." Financial Interview, *supra* note 32, at 3, No. 13.

42. Because of the dominance of savings and loan associations in the residential lending market, the decisional processes described below are most typical of savings and loan associations, although the processes discussed are not materially different in other contexts.

43. U.S. COMMISSION ON CIVIL RIGHTS, MORTGAGE MONEY: WHO GETS IT? A CASE STUDY IN MORTGAGE LENDING DISCRIMINATION IN HARTFORD, CONNECTICUT 9 (1974) [hereinafter cited as HARTFORD REPORT]. This report includes data from staff interviews, conducted in 1972 and 1973, of "real estate brokers, lenders, home buyers, public interest groups, and Federal and city housing specialists." *Id.* at n.9. It includes interviews of 10% of the real estate firms in Hartford, including 80% of the black-owned firms. *Id.* at n.11. The report also refers to many other statistical and analytical sources from which it draws its composite picture of lending in Hartford, Connecticut—a picture which it considers to be typical of other metropolitan areas throughout the country. *Id.* at 4.

44. Commercial banks generally indicated that most of their home mortgage custom-

common method lenders use for soliciting residential mortgage applications is courting real estate brokers and builders, keeping them generally informed of current terms and conditions for mortgages.⁴⁵ In order to complete sales of property as expeditiously as possible, brokers try to ensure that the loan applicants they bring to the financial institutions will be acceptable. If brokers avoid presenting a large number of applicants whom the lenders refuse, they save the lending institution processing costs and thereby maintain a good business relationship.⁴⁶

In testing the buyer's acceptability, brokers try to apply the criteria they think the lenders apply, although they generally have no way of knowing what the precise standards of the lender are (if precise standards in fact exist).⁴⁷ Brokers are more skeptical of the income of blacks than of whites and automatically run credit checks on minority families, but generally not on white families.⁴⁸ To show their value to the lending institution, brokers also tend to be conservative in their referrals. Despite the distortions in the class of potential buyers that this screening causes, there is evidence that at least some lending institution executives expect brokers to do an initial screening for financial suitability.⁴⁹

2. *The Lending Institution*

In the majority of lending institutions, the applicant-buyer first meets with a loan officer. The loan officer may informally screen the applicant to determine whether it will be worthwhile for the potential borrower to make a formal application.⁵⁰ While most applicants would welcome an objective prescreening to save themselves the application fee if they will be refused anyway, the screening may in fact be based only on subjective feelings rather than objective criteria.⁵¹ When one considers that the vast major-

ers are present or previous customers, or walk-in customers who are shopping for terms. Only two of eight commercial banks indicated that they solicit residential mortgage applicants at all.

45. The second most common method of solicitation mentioned was advertising in newspapers and magazines. The question asked was: "Do you actively solicit home mortgage applicants?" Financial Interview, *supra* note 32, at 1, No. 2. If the answer was affirmative, the next question asked was: "How do you solicit home mortgage applications?" *Id.*, No. 2a.

46. See HARTFORD REPORT, *supra* note 43, at 10-12.

47. See notes 50-67 *infra* and accompanying text.

48. HARTFORD REPORT, *supra* note 43, at 10.

49. *Id.* at 11-12.

50. *Id.* at 12-13.

51. *Id.*

ity of loan officers are white,⁵² the impressions on which potential applicants may be screened out may be based as much on race—of the applicant and of the residents of the area in which the applicant intends to purchase a home—as on more objective criteria, such as creditworthiness and the appraised value of the home.

If applicants pass the informal screening, a formal application is taken that asks for specific information from the applicant. The process continues with a credit check and an appraisal of the property to be mortgaged. Financial institution representatives indicated that they investigate both the applicant and the property when they consider a residential mortgage application.⁵³ According to the interview responses, the applicant is considered by most institutions to be of more importance than the property; as one representative pragmatically observed, “I’ve never seen a house make a payment yet.”⁵⁴ The applicant’s income is analyzed in terms of job stability and ability to meet payments, and a check is made of the applicant’s credit record.

Creditworthiness, which the loan officer determines, includes many subjective judgments. If the lending institution simply uses information from a credit bureau, it is accepting judgments made by creditors without learning any of the information on which the judgments are based.⁵⁵ Additional criteria used to determine the acceptability of an individual for a loan often include arrest records and history of previous home ownership. These factors may result in a discriminatory effect on minorities, and have questionable relevance to the applicant’s creditworthiness.⁵⁶

The value of the property which will be the security for the loan is also determined. A financial institution will either use its own appraiser or will contract with an independent appraiser to

52. For example, all representatives of financial institutions in the interview population were white, with the sole exception of one black-run savings and loan association and one black-run commercial bank. See also Swindell, *Sex Bias Charged at Big Banks*, *The Plain Dealer* (Cleveland), Feb. 20, 1978, § D, at 10, col. 2 (indicating that in two Cleveland commercial banks for which information was available, “less than 2% of the officer and manager positions were filled with black men and the employment of black women in those categories was so low that it could not be reported statistically. . .”).

53. The question asked was: “What factors influence you the most in your decision to approve a residential loan?” Financial Interview, *supra* note 32, at 1, No. 3a.

54. Quotation from interview; not attributed in order to maintain confidentiality of respondents.

55. HARTFORD REPORT, *supra* note 43, at 15–16.

56. *Id.* at 16.

determine the value of the home.⁵⁷ The two most important criteria used to appraise the residential property are first, the price of other similar properties recently sold in the area and second, the condition of the particular property. Also considered by some institutions are the location and the age of the property. The questions on the Federal Home Loan Mortgage Corporation (FHLMC) Form 465-8/74 suggest the type of information an appraiser considers.⁵⁸ The appraisal provides several opportunities for the subjective bias of the appraiser to be included in the final valuation. For instance, form questions ask for an assessment of "neighborhood compatibility" and "protection from adverse influences."⁵⁹ These designations may relate to concepts of land use, such as the protection of single family residences by zoning which excludes multifamily or commercial buildings. However, appraisers also include concepts like "neighborhood homogeneity" and "population homogeneity,"⁶⁰ allowing for a consideration of the racial characteristics of the community. Moreover, a presumption of an inevitable neighborhood life cycle is built into the question whether the "neighborhood trend" is "improving, stable, or declining."⁶¹ Improvement, stability, and decline are words often used to communicate racial information, with stability implying no change in racial composition and decline implying an influx of racial minorities into a previously white area.

Thus, appraisal and creditworthiness, terms that sound objective, are determined in ways which permit less than unbiased measurement. After the application, appraisal, and credit check are complete, the loan officer decides whether to recommend that the institution make a loan. In some cases where the loans do not exceed a certain figure, the loan officer may make the final decision. In most cases, however, the loan officer's decision is re-

57. Appraisers are nearly always white and have been found to consider race in their reports. *Id.* at 16 n.24.

58. In fact, because so many mortgages originating with local financial institutions are bought and sold on the secondary mortgage market, which includes FHLMC, the FHLMC form is a model that appraisers follow. For an overview of the secondary mortgage market, see Earthman, *Residential Mortgage Lending: Charting a Course Through the Regulatory Maze*, 29 VAND. L. REV. 957, 973-78 (1976).

59. *E.g.*, Appraisal Report—Individual Condominium or PUD Unit, FHLMC Form 465-8/74, at 2.

60. E. RAMS, RAMS' REAL ESTATE APPRAISING HANDBOOK 264 (1975).

61. *E.g.*, FHLMC Form, *supra* note 59, at 2. A neighborhood life cycle ending in decline is inevitable because such inevitability is assumed by actors in the home-lending process. This becomes part of the self-fulfilling prophecy of neighborhood decline. *See* text accompanying notes 72-74 *infra*.

viewed by a loan committee, composed of senior officers of the institution. Interviews indicated that recommendations to the committee are almost always accepted.⁶²

The reason for the consistent acceptance may be not only that the loan officers know and follow the institution's policies and guidelines, but also that the loan officer is expected to err on the side of conservatism. That is, the loan officer will be more likely to refuse a loan than to recommend the loan to a committee composed of his superiors, whose approval he is seeking for the progress of his own career. If the loan officer feels the loan committee has biases in a certain direction, those biases may be magnified by the loan officer's self-interest in preventing any questionable loan applicant from being considered by the senior officers.⁶³

As noted above, the loan committee and senior officers (who generally compose the loan committee) play an important role in determining whether or not an applicant gets a loan. The representatives of financial institutions in Cuyahoga County described lending policies and decisions which are probably typical of other areas. The boards of directors or bank officers set policy, including loan limits, interest rates, and percentage of funds to be invested in residential loans.⁶⁴ These policies are coupled with general directives against discrimination or otherwise breaking the law. The loan officer and the real estate broker apply these policies to their own advantage, within the wide discretion allowed by the general directives.

In addition to setting policy, the senior officers make final decisions on individual loan applications. In interviews, many indicated that because they review each loan application individually, they were unaware of their lending pattern until they analyzed the information that they provided to comply with the HMDA.⁶⁵ Again, subjective biases may be exercised at this highest level of discretionary review. But if the screening process as described above has been effective, there will be little need for the senior

62. The question which elicited this response was: "Would you please explain in as much detail as possible the procedure your institution follows in evaluating and approving or rejecting each home mortgage application?" Financial Interview, *supra* note 32, at 2, No. 5.

63. See HARTFORD REPORT, *supra* note 43, at 13.

64. The question asked was: "How are lending policy decisions made in your institution?" Financial Interview, *supra* note 32, at 2, No. 6.

65. 12 U.S.C. §§ 2801-2809 (1976). For other information that financial institutions learned from their disclosure statements, see note 160 *infra* and accompanying text.

officers to refuse loans on the basis of discriminatory criteria, since those loans that they would refuse for discriminatory reasons have been already screened out by combinations of bias at preceding levels of the home buying process.

Another important factor which is considered by the financial institution when a person applies for a mortgage on a house is how salable the mortgage will be on the secondary mortgage market. It is here that the FHLMC appraisal forms and application forms become important because they indicate the standards for acceptability on the secondary mortgage market.⁶⁶ The importance of the secondary market lies in the role it plays in encouraging a national rather than a local money market. Interviews indicate that almost all the depository institutions deal with the secondary mortgage market to some extent. The degree of their involvement varies tremendously and is a function of policy decisions of the corporation. The involvement of some is mostly in selling locally originated mortgages in order to have more money available for loans. Others primarily buy mortgages for investment purposes. Still others enter the market only occasionally as particular needs arise.

But as long as a financial institution does deal with, or in the future may deal with, the secondary mortgage market, then that institution is not as free to establish its own criteria for deciding when to make or not make a loan. The guidelines established by the secondary market for acceptable loans provide the minimum standards of acceptability. It is necessary, therefore, to prevent bias from being present or permitted at this level.

D. *Summary*

By the time a family purchases a particular home, the family's choice has been channeled and limited by many factors in addition to what the family needs, wants, and can afford. The decision as to what house that family may buy has been made by a series of people, including the seller, the real estate broker, the loan officer, the appraiser, the institutional officers, and those involved in the secondary mortgage market. Many levels of individual judgments allow considerable subjectivity and tremendous potential for discrimination against particular applicants and against particular neighborhoods. Each decision can have a cumulative effect with the other decisions so that, whether intended

66. See note 58 *supra*.

by the individual decisionmakers or not, the end result may be to effectively deny mortgage money to groups of individuals and to neighborhoods, with no business reason (as compared to convenience) to justify the impact.

II. REDLINING

A. *Definition*

Redlining occurs when financial institutions will not lend in specific geographic areas. This is the consensus of housing organizations and financial institutions in Cuyahoga County,⁶⁷ and is consistent with definitions in the literature.⁶⁸ This bare bones definition does little, however, to explain how redlining happens, why it is of public concern, and what its justification may be.

Redlining is a series of lending decisions on a continuum from mild increased costs for individual loans to complete refusal to lend in definite areas. Reports of how redlining occurs include a large variety of techniques which financial institutions use to discourage loans or to cover perceived increased risks, in addition to flat-out refusal to lend. In hearings before the Senate Committee on Banking, Housing and Urban Affairs, when the Committee was considering the Home Mortgage Disclosure Act of 1975, Illi-

67. Over 80% of both financial institutions and housing organizations included this general concept in their definitions of redlining. In addition, one housing organization and one financial institution identified redlining as lending on poor terms, while two housing organizations qualified the definition by saying redlining is granting few or no conventional loans in an area. One housing organization said a redlined area was one which was not getting at least 50% of its savings deposits returned in loans.

Four financial institutions said that redlining does not exist, or that they did not know what it was, or that it was a term that community groups and the media use to blame financial institutions for problems. One said redlining is the refusal of insurance companies to grant fire insurance in an area. The term "redlining" is purported to have originated from the practice of drawing a red circle on a map around areas in which insurance companies would not issue policies. The practice of not providing insurance is still occurring and is a form of redlining different from the mortgage redlining discussed.

68. See, e.g., Wisniewski, *Mortgage Redlining (Disinvestment): The Parameters of Federal, State, and Municipal Regulation*, 54 J. OF URB. L. 367, 367 (1977) (Redlining is defined as "the denial of mortgage loans in a particular geographic area for home purchase, expansion, or remodeling, regardless of the credit of the applicant or quality of the property. . . ."); Note, *Urban Housing Finance and the Redlining Controversy*, 25 CLEV. ST. L. REV. 110, 110 (1976) ("While the essence of redlining is geographical discrimination in home loans, most definitions of redlining fall into two general categories." These are "racial redlining" and "economic redlining."). Redlining is also seen as a "principal tactic in disinvestment," in that it is "a series of progressive steps by which area lending institutions extricate themselves from neighborhoods they predict will deteriorate." A. NAPARSTEK & G. CINCOTTA, *URBAN DISINVESTMENT: NEW IMPLICATIONS FOR COMMUNITY ORGANIZATION, RESEARCH, AND PUBLIC POLICY* 8 (1976).

nois Governor Dan Walker listed the following eleven different ways in which redlining may take place:⁶⁹

1. Requiring down payments of a higher amount than are usually required for financing comparable properties in other areas;
2. Fixing loan interest rates in amounts higher than those set for all or most other mortgages in other areas;
3. Fixing loan closing costs in amounts higher than those set for all or most other mortgages in other areas;
4. Fixing loan maturities below the number of years to maturity set for all or most other mortgages in other areas;
5. Refusing to lend on properties above a prescribed maximum number of years of age;
6. Refusing to make loans in dollar amounts below a certain minimum figure, thus excluding many of the lower-priced properties often found in neighborhoods where redlining is practiced;
7. Refusing to lend on the basis of presumed "economic obsolescence" no matter what the conditions of an older property may be;
8. Stalling on appraisals to discourage potential borrowers;
9. Setting appraisals in amounts below what market value actually should be, thus making home purchase transactions more difficult to accomplish;⁷⁰
10. Applying structural appraisal standards of a much more rigid nature than those applied for comparable properties in other areas;
11. Charging discount "points" as a way of discouraging financing.⁷¹

Additional examples of subtle redlining practices include committing mortgage money to future developments, thus restricting the present supply available for individuals, and relocating financial institutions, making them less accessible to applicants in the former location.⁷²

B. *The Effects of Redlining*

Redlining is an important phenomenon because of its effects. Many commentators consider redlining to be a self-fulfilling

69. *Hearings on S. 1281 Before the Senate Comm. on Banking, Housing and Urban Affairs*, 94th Cong., 1st Sess. 35 (1975) (footnotes added) [hereinafter cited as *Hearings*].

70. See notes 58-61 *supra* and accompanying text.

71. Discount points are a means to avoid upper limits on interest rates imposed by the law by requiring that the buyer actually pay higher interest rates than are shown on the record. For a more complete description of the practice, see Note, *supra* note 34, at 999 n.67.

72. See Note, *supra* note 31, at 73.

prophecy of neighborhood decline.⁷³ When financial institutions consider an area to be a greater risk than another area—or alternatively, when they perceive one area to be more attractive for investment than another area—their decisions on lending will reflect those perceptions. As noted earlier, various decisionmakers within financial institutions have great latitude in choosing from the various applicants and in selecting the properties they want to accept as collateral. In addition, the policymakers can set priorities for lending that will reflect unfavorably on particular areas.

Once financial institutions become more or less reluctant to lend in an area, resulting in decisions that connote a perceived loss in investment attractiveness, a process sets in that almost inevitably leads to progressive decline and deterioration, resulting in disinvestment of the entire neighborhood. This process characteristically occurs in stages over a period of several years. Six phases of neighborhood deterioration are described by a Cleveland housing organization.⁷⁴ First, a healthy neighborhood exists with strong demand for housing and readily available financing. Second, subtle symptoms of redlining appear, such as changes in loan terms, as local lenders begin to move their credit elsewhere because of a “funny feeling” about the neighborhood. Third, redlining by neighborhood lenders becomes obvious as loans for purchase and home improvement are refused. This results in an inability to maintain present properties; an exodus of businesses and of socially mobile residents begins. Fourth, the larger downtown institutions also refuse to lend. With only FHA insured mortgages available speculators will “turn over” the area. Fifth, spiraling deterioration takes hold with abandoned housing, increased rentals, no maintenance, no property insurance, and declining city services. Sixth, urban renewal moves in to squeeze out the poor with housing for the well-to-do.

Similar results from redlining were described by other Cuyahoga County housing organizations when they were asked what happens to a redlined area. Almost one-half of the organizations replied that maintenance of houses virtually ceases and

73. E.g., Bradford & Rubinowitz, *The Urban-Suburban Investment-Disinvestment Process: Consequences for Older Neighborhoods*, 422 ANNALS 86 (1975).

74. Citizens Action Program, *The Phases of Neighborhood Deterioration* (Mimeographed paper received from a housing organization in the survey). The same sequence of disinvestment is described in Reinvestment Committee of Milwaukee Alliance of Concerned Citizens, *Red-lining on Milwaukee's Westside*; see *Hearings, supra* note 69, at 293, 295-300.

that people move out.⁷⁵ This is the third phase of the process of deterioration described above—the first step after local lenders begin to redline. One-fifth to one-quarter of the organizations said that neighborhoods decline generally, fewer city services are provided, much vacant and vandalized housing appears, and much speculation occurs. As noted previously, and confirmed by two organizations, the last two symptoms may often occur in conjunction with an influx of FHA loans. Organizations also mentioned the phase five characteristics of an increased number of rentals and increased population density.⁷⁶ The housing organizations drew a composite picture: as money is pulled out of an area by the banks' refusal to invest, the banks' expectation of deterioration is fulfilled. The area loses its ability to attract homeowners as money for housing becomes less available. Because houses cannot be easily bought and sold, their market value goes down. Then absentee owners buy the houses and put them to other uses until they become virtually valueless for private use.

C. *Why Does Redlining Occur?*

A brochure that a savings and loan association distributes to its customers indicates the choice that it perceives itself compelled to make when deciding whether or not to lend.⁷⁷ It can either make a loan considered risky according to its discretionary standards, or refuse to loan, thereby maximizing the association's profits at the expense of the community's financial health. The institution "must weigh the *social merit* of any loan application against our *fiduciary responsibility* to protect the value of your savings—and the savings of thousands of others. Our obligation to our savers must come first."⁷⁸ In practical effect, a loan that might risk depositors' savings must be refused. The institutions' representatives are naturally most concerned about their fiduciary responsibilities to their depositors and stockholders. They react to those relatively well-defined responsibilities first and wait for government regulatory agencies to define more clearly their legal ob-

75. Additional responses indicated that in general, money is drawn out of the area, the tax base diminishes as property fails to appreciate in value, bank withdrawal fulfills the expectation of deterioration, and the area loses its ability to attract people.

76. Each of these characteristics was mentioned by two organizations.

77. State Savings and Loan Company, Report to Savers . . . About Mortgage Loan Disclosure and our Lending Policies (1976).

78. *Id.* A lender in the present survey remarked that "we cannot convert the banking business into a social agency." He added that instead perhaps the definition of good business judgment ought to be changed.

ligations in areas of social concern.⁷⁹

One measure lenders use to evaluate the risk to investment capital is the foreclosure rate. If the borrower defaults on the loan, the ultimate recourse to recover the money lent is to foreclose. Because foreclosure entails considerable cost to the institution for administrative and legal fees, lenders interviewed indicated that they try to avoid foreclosure whenever possible, even when a loan is in serious default.⁸⁰ Two-thirds of the lenders interviewed experienced a foreclosure rate during the last fiscal year of considerably less than one percent. An additional twenty percent had no foreclosures at all.⁸¹

In fact, many see the practice of redlining as beneficial to some people or institutions. Most housing organizations and some financial institutions in the Cuyahoga County survey indicated that redlining benefits someone.⁸² Commercial banks and savings and loan associations and their depositors were mentioned most often as the beneficiaries.⁸³ Additional beneficiaries mentioned were insurance companies, mortgage companies,⁸⁴ real estate brokers,⁸⁵ speculators,⁸⁶ and the FHA (in previous years).⁸⁷

79. For a brief analysis of what those social obligations may be at this time, see notes 118-25 *infra* and accompanying text.

80. This hesitancy is in marked contrast to swift FHA foreclosure where the costs of foreclosure are paid by the government. See note 38 *supra* and accompanying text.

81. One savings and loan association, which gives no indication that its profitability is jeopardized, continues to concentrate its lending in the older areas of the county where its branches are located. It stated that its foreclosure rate is "a little higher than average" because of the lending it does in "mostly dilapidated areas" of the county, but gave no basis for its comparison. A study conducted in Pittsburgh indicates that loans within the central city are generally more risky than loans to the outlying areas. Williams, Beranck, & Kenkel, *Factors Affecting Risk in Urban Areas—A Pittsburgh Prototype Analysis, Hearings, supra* note 69, at 628.

82. Eighty percent of the housing organizations and twenty-four percent of the financial institutions indicated this.

83. Ten of the twelve housing organizations which indicated that someone benefits, mentioned one or more of these categories, as did five of the seven financial institutions.

84. Mortgage companies, as a source of nonconventional capital for buying homes, are considered by many to be speculators, looking for the "fast buck." They do not operate extensively in an area until some degree of redlining by conventional lenders has made their financing necessary. See, e.g., National Training and Information Center, Federal Housing Administration: *The American Nightmare* (1976).

85. Real estate brokers profit by selling houses. When a large volume of houses are sold quickly in an area because of a quick turnover of FHA housing (often the major source of residential financing because of redlining), the real estate brokers profit from the increased sales.

86. Speculators include those who are looking to make quick profits in any stage of the home buying process, without regard for the consequences to the neighborhood.

Lenders perceive risks when they are asked to lend in certain areas. Although concerned citizens may say that financial institutions which redline cause urban disinvestment, the profile that financial institutions in the survey gave of areas in which they would expect redlining to occur indicates that the areas where they will not lend have already begun to be disinvested, in the sense of not having sufficient money to prevent deterioration.⁸⁸ For instance, lack of maintenance was the factor mentioned by almost one-half the lenders.⁸⁹ High crime, vandalism, or fires

When conventional kinds of financing are not available, however, speculators may be the only source of financing.

87. One institution indicated that this was an expedient means of screening loans. In fact, FHA standards used to *require* racial redlining and racially restrictive covenants. U.S. FEDERAL HOUSING ADMINISTRATION, UNDERWRITING MANUAL: UNDERWRITING AND VALUATION PROCEDURE UNDER TITLE II OF THE NATIONAL HOUSING ACT (1938).

88. The question asked was: "What are the major characteristics of an area in which one would expect redlining to occur?" L. McKinney & P. Pap, Community Organizations Interview Form at 10, No. 20 (1977) (unpublished questionnaire on file in Case Western Reserve University School of Law Library); L. McKinney & P. Pap, Financial Institutions Interview Form at 5, No. 24 (1977) (unpublished questionnaire on file in Case Western Reserve University School of Law Library). Nine of the twenty-nine respondents to this question indicated either that redlining does not exist or that they did not know where it would occur. The responses may be graphically illustrated as follows:

COMPARATIVE IMPORTANCE OF FACTORS
ASSOCIATED WITH THE EXISTENCE OF REDLINING

FINANCIAL INSTITUTIONS Rank (percent mentioned)	FACTOR	HOUSING ORGANIZATIONS Rank (percent mentioned)
1 (48%)	lack of maintenance	4 (27%)
2 (31%)	high crime, vandalism, fires	not mentioned
3.5 (17%)	large number renters, absentee landlords	4 (27%)
3.5 (17%)	poor city services	4 (27%)
5.5 (14%)	poorer residents	2 (60%)
5.5 (14%)	older properties	6 (13%)
8 (10%)	ethnically or racially polarized or changing	1 (67%)
8 (10%)	vacant and vandalized homes	6 (13%)
8 (10%)	lack of pride; poor social cohesion	not mentioned
Not mentioned	older residents	6 (13%)

89. See table, note 88 *supra*.

were important to almost one-third.⁹⁰ A large number of renters, absentee landlords, and poor city services (including poor schools) were cited by one-sixth of the respondents.⁹¹ Older properties were important to one-seventh, as were poorer residents.⁹² Factors mentioned by any three of the financial institutions were: vacant and vandalized homes, lack of pride or poor social cohesion of the residents, and an ethnically or racially polarized or changing neighborhood.⁹³ All of these factors describe neighborhoods which have begun to decline.

Interestingly, housing organizations articulated a different community profile when asked where they would expect redlining to occur.⁹⁴ Racial or ethnic polarization or change was mentioned by two-thirds of the housing organizations, as compared to only three financial institutions.⁹⁵ Poor residents were also mentioned by almost two-thirds of the housing organizations, as compared to one-seventh of the financial institutions.⁹⁶ Lack of maintenance, poor city services, and a large number of renters and absentee landlords were next in aggregate number of those factors mentioned, but they were well below the first two categories. Each of these was among the six factors most often mentioned by the financial institutions.⁹⁷

Thus, the financial institutions' composite description of areas in which they expected redlining included poorly maintained homes, high incidence of crime destructive to property, large numbers of renters with less incentive to maintain their residences,⁹⁸ and little support from the city to maintain the quality of living. Presumably, these factors are what lenders consider when they make a decision on whether to loan in a particular area.

In comparison, the housing organizations' descriptions focused

90. *See id.*

91. *See id.*

92. *See id.*

93. Other factors mentioned by only one or two institutions were whether the area was a complete slum, whether it was changing from residential to industrial, whether it had a high density, and whether there was insurance available. None of these factors were mentioned by any of the housing organizations.

94. *See table, note 88 supra.*

95. *Id.*

96. *Id.*

97. *Id.*

98. *See Note, Attacking the Urban Redlining Problem, 56 B.U. L. REV. 989, 998 (1976).*

more on the residents than on the properties.⁹⁹ In redlined areas the residents were racially or ethnically polarized or in rapid transition, creating anxieties in the neighborhood. Also, they were poorer than those in nonredlined areas. The other characteristics of the neighborhood were similar to those described by the financial institutions, with one exception. Crime, the factor most often cited by the financial institutions, was mentioned only tangentially by housing organizations; vandalism was mentioned only as a corollary to the increased incidence of vacant houses.

All these factors, however, are held out by financial institutions to justify decisions not to lend in an area. The perceived high rate of property crime is a risk to the real property which is collateral for the loan. Also, lack of maintenance in the surrounding area tends to lower the appraised value of the house to be purchased, even if the particular structure is well maintained. Renters and absentee landlords have less incentive to maintain their housing than do resident homeowners; and, as maintenance deteriorates, the neighbors' incentive to maintain decreases as the value of their houses is reduced by those that are poorly maintained. In addition, older properties require more maintenance, and when families are poorer, they have fewer resources to meet the increased costs of upkeep. Poor city services also make the area less attractive than areas where services are better and the quality of living is improved by better safety, sewers, and schools. The unattractive neighborhood lowers the sale value of properties and affects the appraised value of the particular property the applicant wants to buy.

The characteristics that were given varying emphasis by the financial institutions and the housing organizations are not necessarily mutually exclusive. While the emphases are different, the picture that each gives could easily contain the elements that the other depicts. This observation is supported by the fact that, when asked about redlining in Cuyahoga County, there was general consensus in the description of areas where it occurs.¹⁰⁰ While all respondents did not describe exactly the same locations,

99. This is interesting, considering the lenders' professed preoccupation with the borrowers. See note 54 *supra* and accompanying text.

100. Forty-eight percent of the financial institutions indicated that redlining does not exist or that they do not know whether it exists in Cuyahoga County. All housing organizations responded that it does exist, and all but one said it occurs in their organizational service areas. The geographical areas of redlining were described by the financial institutions' answers to several questions.

the areas described were in parts of the county which are predominantly black or interracial. No respondents suggested that identifiably white areas are being redlined. Thus, while financial institutions did not mention race as an important characteristic in a redlined area, race is an obvious factor. In fact, in view of the subjective judgments that are made by individuals in the institutional decisionmaking sequence,¹⁰¹ the race of a neighborhood may encourage the decisionmaker to presuppose the existence of the other characteristics.

Yet, whatever the reason for redlining, because the process has such a significant impact on large sections of our country's cities, the question must be asked whether these private decisions by quasi-public lending institutions may be permitted to continue to cause the public the harm that results. Senator Proxmire, chairman of the Senate Committee on Banking, Housing and Urban Affairs, highlighted the public aspect of lending institutions when he observed that they "are not chartered simply to make as much money as they can. . . . They have certain privileges, such as federal insurance and a partial monopoly. In exchange for these privileges, they have obligations. One such obligation is to serve their service area."¹⁰²

D. *The Legality of Redlining*

There is current federal law which may be used to penalize those who redline on the basis of race. Recently a federal district court¹⁰³ held that refusal to make loans in areas in which minority groups are concentrated violates Title VIII of the Fair Housing Act of 1968.¹⁰⁴ Title VIII proscribes racial discrimination in the sale or rental of housing¹⁰⁵ and in the financing of housing,¹⁰⁶ and protects against interference with an individual's right to voluntary, interracial association.¹⁰⁷ The district court also found that defendant's actions, on a motion for summary judgment, violated Title VI of the Civil Rights Act of 1964,¹⁰⁸ which prohibits discrimination by any program or activity receiving federal financial

101. See notes 42-66 *supra* and accompanying text.

102. 121 CONG. REC. 25161 (1975) (remarks of Sen. Proxmire).

103. *Laufman v. Oakley Bldg. & Loan Co.*, 408 F. Supp. 489 (S.D. Ohio 1976).

104. 42 U.S.C. §§ 3601-3631 (1970 & Supp. V 1975).

105. *Id.* § 3604 (Supp. V 1975).

106. *Id.* § 3605.

107. *Id.* § 3617 (1970).

108. *Id.* § 2000d (1970 & Supp. V 1975).

assistance. Because the defendant building and loan association was a member of the Federal Home Loan Bank Board system, the 1964 Civil Rights Act was held applicable.

The Civil Rights Act of 1866¹⁰⁹ may be another statutory basis for attacking financial institutions which redline. Its language states that all citizens have the same rights as white citizens to buy real property. This section has been interpreted by the Supreme Court to prohibit "all racial discrimination, private as well as public, in the sale or rental of property."¹¹⁰

A number of states and cities have instituted legislation or regulations to control redlining.¹¹¹ For example, an Illinois statute¹¹² specifically prohibits denying or varying the terms of a loan "on the basis that a specific parcel of real estate offered as security is located in a specific geographical area."¹¹³ This is a classic definition of redlining. Under this statute, a financial institution also may not "utilize lending standards that have no economic basis and which are discriminatory in effect."¹¹⁴ This second proscription would be a difficult standard to use to control lenders, since financial institutions argue that any change in the present process would prevent them from carrying out sound economic procedures. The more appropriate question may be whether the economic basis is sufficiently strong to justify the effect of the lending standards.

A practical difficulty with statutes allowing private causes of action to control redlining is the delay involved in litigation. An individual who brings suit because he was refused credit to purchase a house will probably not be able to buy that particular house by the time the suit has been successfully concluded. The

109. *Id.* § 1982 (1970).

110. *Jones v. Alfred H. Mayer Co.*, 392 U.S. 409, 413 (1968) (emphasis in the original). In this landmark case, the Supreme Court found that the 1866 statute prohibited discrimination by private, as well as state actors. Previously, the statute had been read to apply only to state action.

An alternate approach to attacking redlining, using § 1 of the Sherman Act, 15 U.S.C. § 1 (1976), focuses on the anticompetitive rather than the racial effects of redlining activities. Liability under this statute would result from finding a combination or conspiracy to restrain trade or commerce. Comment, *Redlining: Potential Civil Rights and Sherman Act Violations Raised by Lending Policies*, 8 *IND. L. REV.* 1053 (1975).

111. For the details of various legislative and regulatory efforts, see Wisniewski, *supra* note 68, at 394-402.

112. *ILL. REV. STAT.* ch. 95, §§ 201-307.

113. *Id.* § 304(a). The problems of proving an allegation based on the statutory language are immense.

114. *Id.* § 304(d).

time between the refusal of a loan application and the conclusion of a suit will exceed the number of days generally allowed for securing financing in a purchase agreement. If financing is not found within that time, the purchase agreement is void and the seller may sell to anyone else. Since the seller is not responsible for the buyer's inability to obtain credit, there would be no reason to cause the seller additional injury by preventing the sale of the house to another until the litigation is resolved. Thus, one important incentive for filing suit against the financial institution for redlining is removed. This is particularly true if there is a chance of obtaining financing for another house in another location. After all, the basic goal of the prospective buyer is to actually purchase a house in whatever way is practical.

The Housing Act of 1949,¹¹⁵ the Civil Rights Act of 1964,¹¹⁶ and the Fair Housing Act of 1968¹¹⁷ all mandate that departments and agencies of the federal government use their powers to facilitate and further the acts' purposes. At present, this mandate is not being fulfilled in the area of redlining. Four federal agencies regulate the financial institutions which provide most of the funds for home financing in this country. They are the Comptroller of the Currency, the Federal Home Loan Bank Board, the Board of Governors of the Federal Reserve, and the Federal Deposit Insurance Corporation.¹¹⁸ In addition, the government has established quasi-public instrumentalities to promote liquidity in the home mortgage market.¹¹⁹ The federal government is also involved in private, nonsubsidized residential lending by insuring mortgages through the FHA and the Veterans Administration (VA).¹²⁰ Loans insured by the FHA provide an opportunity to obtain home

115. 42 U.S.C. § 1441 (1970).

116. *Id.* § 2000d-1 (Supp. V 1975).

117. *Id.* § 3608(c) (1970).

118. The respective duties of these agencies have been summarized as follows:

The Comptroller of the Currency regulates national banks, the Federal Reserve Board regulates state-chartered commercial banks which are members of the Federal Reserve System, and the Federal Deposit Insurance Corporation regulates the remainder of the state-chartered commercial banks. The Federal Home Loan Bank Board (FHLBB) comprehensively regulates federally-chartered savings and loan associations that insure deposits with the Federal Savings and Loan Insurance Corporation. Of all federal regulatory agencies, the FHLBB has the greatest impact upon urban home loans.

Note, *Urban Housing Finance and the Redlining Controversy*, 25 CLEV. ST. L. REV. 110, 123 (1976).

119. See Earthman, *Residential Mortgage Lending: Charting a Course Through the Regulatory Maze*, 29 VAND. L. REV. 957, 973-78 (1976).

120. See notes 36-38 *supra* and accompanying text.

financing when conventional financing is not available, but because of the way FHA financing has been administered it has contributed to, rather than alleviated, many of the problems associated with redlining.¹²¹

Regulations by the regulatory bodies have begun to address the redlining problem. The Federal Home Loan Bank Board has issued policy statements and regulations which indicate that lending institution practices that have the effect of discrimination violate the law, even if there is no intent to discriminate.¹²² Nevertheless, the regulations allow standards with discriminatory effect if they achieve "a genuine business need."¹²³ The Federal Reserve Board has issued a statement that it will allow an institution to "take an active role in the quest for solutions to the nation's social problems" by engaging in "projects designed primarily to promote community welfare."¹²⁴ It is not apparent from this statement whether socially responsible investment activity is an affirmative obligation of an institution, but it is at least permissible. The four regulatory agencies have also been working together to collect information about the problems involved in fair housing.¹²⁵

The regulatory agencies have the power to ensure that financial institutions serve their communities. Since they have broad regulatory power over the major lending institutions in the country, they should also assume the major responsibilities for correcting practices that clash with national housing objectives as declared by Congress. At least partially because the regulatory agencies have not been active in this area, Congress passed the 1975 Home Mortgage Disclosure Act to deal more specifically with the problem of redlining.¹²⁶

121. See notes 36-41 *supra* and accompanying text.

122. 12 C.F.R. § 531.8 (1975). As the *Laufman* court indicated, these Federal Home Loan Bank Board regulations were developed to interpret the Fair Housing Act of 1968. 408 F. Supp. 489, 494 (S.D. Ohio 1976).

123. 12 C.F.R. § 531.8(b) (1975) (amendments to 12 C.F.R. §§ 528 and 531.8 became effective July 1 and September 1, 1978, respectively, 43 Fed. Reg. 22, 332 (1978)). See note 186 *infra*.

124. 12 C.F.R. §§ 225-227 (1976).

125. See, e.g., COMPTROLLER OF THE CURRENCY, FAIR HOUSING LENDING PRACTICES PILOT PROJECT, SURVEY C APPROACH (1975).

126. 12 U.S.C. §§ 2801-2809 (1976).

III. THE HOME MORTGAGE DISCLOSURE ACT

A. *The Purpose of the Home Mortgage Disclosure Act*

Congress found that "some depository institutions have sometimes contributed to the decline of certain geographic areas by their failure pursuant to their chartering responsibilities to provide adequate home financing to qualified applicants on reasonable terms and conditions."¹²⁷ The stated purpose of the HMDA is "to provide citizens and public officials . . . with sufficient information to enable them to determine whether depository institutions are filling their obligations to serve the housing needs of the communities and neighborhoods in which they are located."¹²⁸

Section 302(a) of the HMDA reflects Congress' belief that depository institutions have responsibilities under their charter to provide adequate home financing to qualified applicants on reasonable terms and conditions. This legal obligation is based on the fact that these institutions are required to demonstrate that any new office or branch they propose to establish is necessary to meet the conveniences and needs of the local community.¹²⁹ The information to be reported under the HMDA will provide means by which to evaluate whether financial institutions are meeting the bona fide needs of the community in which they were chartered.¹³⁰

This congressional emphasis on the obligation of a depository institution to serve its local community is contrary to other trends in banking law. While governmental regulation of the banking and lending industry has steadily increased over the years, restrictions as to the area in which an institution may operate have eroded.¹³¹ Charters once limited an institution's activities to a 20-mile radius; now the same institution may lend anywhere in the state.¹³² The Federal Home Loan Bank Board has long had the authority to monitor the activities of federal savings and loan associations within their communities, but the Board has never exer-

127. *Id.* § 2801(a).

128. *Id.* § 2801(b). The Uniform Depository Act in Ohio prohibits public officials from making deposit decisions based on disclosure information because of bidding requirements set out in the Act. OHIO REV. CODE ANN. §§ 135.01-09 (Page Supp. 1978).

129. S. REP. NO. 187, 94th Cong., 1st Sess. 11 (1975); see note 102 *supra* and accompanying text.

130. H.R. REP. NO. 561, 94th Cong., 1st Sess. 13, reprinted in [1975] U.S. CODE CONG. & AD. NEWS 2303, 2315.

131. See, e.g., Ohio Am. Sub. S.B. 256, Ohio Branch Banking Bill.

132. OHIO REV. CODE ANN. § 1111.03(A) (Page 1967).

cised this power.¹³³ The financial institutions interviewed, without exception, viewed their primary charter responsibility as protecting the interests of their depositors. None mentioned an obligation to ensure that adequate home financing was available to the residents of the neighborhood in which it was located.

Part of the problem of urban disinvestment may lie in the formidable reputations of the depository institutions. Lenders interviewed in Cuyahoga County frequently asserted that home mortgage and home improvement loans are available to all financially qualified persons who want them. But the bewildering intricacy of lending procedures, supported by popular mythology, as to the requisites of a successful loan applicant, is probably as important as any other single factor in limiting the amount of home loan dollars which flow into our older city neighborhoods. Residents do not think they can get a loan, do not apply for one, and therefore do not get one. The need for community education to dispel these myths is clear. Less clear is the responsibility of financial institutions themselves to provide some of this education. It is perhaps easier and more profitable for lenders to follow the road to new suburban developments for their business. Yet the institutional charters require that they take other considerations into account. Financial institutions have more than one set of obligations and responsibilities.¹³⁴ With the the passage of the HMDA, Congress recognized that

there have been too many instances in which financial institutions have denied credit where it was not necessitated by the responsibility of the institution to vouchsafe the safety of depositor funds. There have been too many instances where arbitrary decisions have been made by financial institutions without even an appraisal. . . . There have been too many instances where home improvement loans, mortgage loans for homes in the \$10,000 to \$15,000 category have not been made because they were not "profitable," not because they were "risky."¹³⁵

The Act requires all depository institutions which are federally licensed or insured and which make federally related mortgage loans, to report publicly the dollar amount and location of all conventional and FHA and VA insured mortgage loans made during

133. H.R. REP. No. 561, 94th Cong., 1st Sess. 13, *reprinted in* [1975] U.S. CODE CONG. & AD. NEWS 2303, 2315.

134. *Id.* at 19, *reprinted in* [1975] U.S. CODE CONG. & AD. NEWS 2320-21.

135. *Id.* at 20, *reprinted in* [1975] U.S. CODE CONG. & AD. NEWS 2321.

the previous fiscal year.¹³⁶ Local residents and community groups may use loan distribution information as a tool to encourage greater investment in their neighborhoods. As the United States League of Savings Associations observed, "Fundamentally what is involved here is that if your disclosure statement creates interest on the part of your savers, the general public and the media, you will be required to justify your lending patterns."¹³⁷ The other side of that coin is well illustrated by two savings and loan associations which have worked in conjunction with local community groups to carry out promotional advertising campaigns in separate Cleveland neighborhoods. These two lenders have set an example for expanding investment in these and other urban areas. Both have received widespread promotion for their "community-mindedness." Such advertising and increased good will may be an added incentive to spur other institutions to lend in older neighborhoods.

Congress anticipated this result in passing the HMDA. It hoped that "once depositors are aware of the lending policies of institutions in their communities, marketplace competition will lead lenders to become more community-minded and mortgage credit will become more plentiful in older neighborhoods."¹³⁸ Any shift in savings patterns would be closely scrutinized by financial institutions and changes in their lending practices would likely result.

B. *Use of the Home Mortgage Disclosure Act by Housing Organizations*

Mortgage loan disclosure statements were required by law to be available for the first time on September 30, 1976.¹³⁹ Cuyahoga County's community housing organizations dubbed

136. The Board of Governors of the Federal Reserve may exempt from federal disclosure requirements any state chartered depository institution within a state which has substantially similar disclosure legislation with adequate enforcement provisions. 12 U.S.C. § 2805 (1976).

137. W. O'Connell, Presenting Mortgage Loan Data to the Public, United Savings League Special Management Bulletin 166, at 1 (July 26, 1976).

138. S. REP. NO. 187, 94th Cong., 1st Sess. 1 (1975). Senator Proxmire stated it even more directly when he explained that "[t]he idea, frankly, is that many customers would favor institutions that kept at least some money in the community." *Hearings on S. 1281 Before the Senate Comm. on Banking, Housing and Urban Affairs*, 94th Cong., 1st Sess. 2 (1975) [hereinafter cited as *Hearings*].

139. 12 C.F.R. § 203.5 (1976).

this momentous occasion "hit day."¹⁴⁰ They identified thirty-five lending institutions active in the county, apportioned these institutions among themselves, and systematically appeared at each institution's main office on that morning.

The symbolic importance of that first "disclosure" was ample incentive for groups to take the time to personally traverse the county collecting disclosure statements. That initial enthusiasm had waned by the second disclosure deadline. Fewer groups helped collect statements, and the process took more than one day. Some institutions were contacted by mail instead of in person. The fact is that mortgage loan disclosure statements are difficult to analyze. Furthermore, once analyzed, the data are inadequate to clearly document redlining. For example, there is no measure of the demand for loans in a particular part of the community at a particular institution. Nearly one-half the housing organizations which analyzed the data agreed that the information provided was insufficient to establish the actual existence of redlining.¹⁴¹ The hours needed to make any sense out of the raw data seem to be wasted when findings derived from the disclosure statements are countered with: "But no one from that part of town asked us for a mortgage loan."

On the other hand, housing organizations do know whether or not people are trying to buy homes in their service area. Community group respondents recounted story after story of persons denied loans because the house was "on the wrong end of the street," "in a risky area," "built before World War II," and so on. Assuming, then, that demand for homes in these areas exists, some groups have used the data provided in the disclosure statements to make several different evaluations of lending practices.

One-half of those who identified redlining as a primary focus of their activity had completed their own analysis of the disclosure

140. When asked: "Were you or was someone in your organization involved in the passage of the Home Mortgage Disclosure Act?," more than half the housing organizations indicated that they were. L. McKinney & P. Pap, Community Organizations Interview Form at 13, No. 27 (1977) (unpublished questionnaire on file in Case Western Reserve University School of Law Library) [hereinafter cited as Community Interview]. Most often this involvement took the form of lobbying public officials on federal, state, and local levels, testifying at public hearings, and generally making contact with public officials, the media, and financial institutions to raise awareness about redlining. For a description of the housing organizations involved in the study, see note 9 *supra* and accompanying text.

141. The questions asked were: "What do you see as the major purpose of the Home Mortgage Disclosure Act? Do you believe that the Act satisfies this major purpose, or do you feel that the Act fails to satisfy this purpose?" *Id.* at 15, Nos. 36 & 37.

data.¹⁴² The simplest and most common comparison made was to note the number of loans made by each financial institution in their service area. Then the number of loans made by each institution in that area was compared from one disclosure period to the next. Some groups looked at financial institutions with branches in their community and compared the number and dollar amounts of mortgage loans made there with the same figures for that institution in neighboring communities. Often the difference between the communities was their racial composition. Home improvement loans in each neighborhood were compared in the same way.

A more sophisticated variation of this measure was created by one housing organization. A rough estimate of the expected number of mortgage loans granted in the community was derived by finding the percentage of dwelling units in the county that were located in the particular inner ring suburb. Then the total number of mortgages granted by each institution in the suburb was compared to those granted in the county as a whole. This percentage was measured against the predictor, to evaluate the adequacy of a specific institution's investment in the community.

A third kind of analysis made by some housing organizations was to compare the number of conventional mortgages to the number of government insured mortgages made by each financial institution on single family homes in the neighborhood. Going one step further, at least one group then compared the number of government insured mortgages in the area to the number of VA and FHA foreclosures. This last measurement was intended to illustrate the special problems a community faces when the incidence of government insured mortgages is high.

Community housing organizations found an imaginative variety of uses for their findings from the mortgage loan disclosure statements.¹⁴³ Apparently, these findings need not be sophisticated to be effective bargaining tools with financial institutions. In turn, most financial institutions interviewed see community housing organizations as central to the process of identifying and deal-

142. The questions asked were: "Have you analyzed the data which you obtained? After analyzing the home mortgage disclosure data, what were your findings?" *Id.* at 14-15, Nos. 35 & 35b.

143. The question asked was: "Did you subsequently use the findings of your analysis for any specific purpose? What was that purpose? How did you accomplish or attempt to accomplish this purpose? What were the results of this?" *Id.* at 15, Nos. 35c-35f.

ing with redlining.¹⁴⁴ A quarter of the financial institutions specifically suggested that neighborhood groups provide the impetus needed for upgrading the quality of city neighborhoods by encouraging home improvements, building community pride, and negotiating with lenders. This may in part be a "pass the buck" approach, but it appears to be backed by a genuine willingness to cooperate on reinvestment programs with neighborhood groups and city officials. This is in keeping with the congressional objective to "provide a vehicle for neighborhood residents, public officials, and financial institutions to enter into partnerships with each other in joint efforts to plan reinvestment strategies for declining neighborhoods."¹⁴⁵ The psychological impact of "disclosure" on lenders may have engendered a willingness to listen to the concerns of community groups. Perhaps the national debate on redlining and the mere passage of the HMDA have gone a long way toward fulfilling the congressional purpose despite inadequacies in the disclosures required by the HMDA.

Nearly all of the housing organizations interviewed reported having met with individual lending institutions to negotiate increased lending in their neighborhoods.¹⁴⁶ Two-thirds of all financial institutions interviewed had had contact with a community group to discuss lending practices and procedures.¹⁴⁷ In eighty percent of these cases, lenders felt that the contact was

144. This statement was in response to the question: "Assuming that one of the purposes of the Home Mortgage Disclosure Act is to encourage reinvestment in residential areas where loans have not been readily available, what suggestions would you have to accomplish that purpose?" L. McKinney & P. Pap, Financial Institutions Interview Form at 9, No. 45 (1977) (unpublished questionnaire on file in Case Western Reserve University School of Law Library) [hereinafter cited as Financial Interview].

145. H.R. REP. NO. 561, 94th Cong., 1st Sess. 14, reprinted in [1975] U.S. CODE CONG. & AD. NEWS 2303, 2315.

146. The questions asked were:

- Has your community group had any contact with lending institutions, with respect to the redlining issue, in the past two years?
- With approximately how many different lending institutions have you had such contact during this two year period?
- With whom were your three most recent contacts?
- Could you please describe your contact with (1, 2, 3), including your intentions prior to the contact, what occurred during the contact, and the results of the contact?

Community Interview, *supra* note 140, at 4, Nos. 14–14c.

147. The questions asked were: "Community groups have increasingly taken an interest in the lending practices of financial institutions in their neighborhoods. Have you had any contacts with a community group? Would you please describe the contact(s)? Would you rate your contacts as being a positive, negative, or neutral experience? Why?" Financial Interview, *supra* note 144, at 8, Nos. 44–44b.

positive.¹⁴⁸ A ten percent negative response can be attributed to the confrontational sit-in style of one community housing organization.¹⁴⁹

Community housing organizations often used these meetings with lenders to inform lenders of their lending practices, as they appeared from the disclosure statements, and to ascertain the institution's concern with lending in the community. These housing organizations often reported back to city government with the aim of encouraging city officials to pressure the financial institutions to increase investment in the neighborhood.¹⁵⁰ Toward this end, housing organizations have made two basic recommendations to city governments in Cuyahoga County: first, that additional city disclosure legislation be considered and second, that city funds be deposited only in financial institutions that have contributed positively to the growth of the community or that have made commitments for increased lending.¹⁵¹

These initial meetings have led, in some instances, to the creation of an ongoing relationship between the lender, the housing organization, and the city. One good example, from a Cleveland suburb, is a city funded committee, composed of representatives of all of the actors in the home delivery system, including real estate agents, appraisers, mortgage bankers, savings and loan officers, and commercial bankers, in addition to community residents and city personnel. This committee monitors lending practices, develops code enforcement programs, initiates redevelop-

148. The questions asked were: "Would you rate your contact with (1, 2, 3), as being a positive, negative, or neutral experience? Why?" *Id.* at 5, No. 14d.

149. Members of this organization occupied the lobby area of one financial institution for an afternoon, after the officers of the institution refused their request for a meeting to discuss lending in their neighborhood. The group brought picnic lunches and transistor radios into the building. They were orderly but of course little work was accomplished that afternoon by the employees of the financial institution.

150. The questions asked were:

- Has _____ had any contact with local, state, or federal public officials or agencies with respect to redlining issues in the past two years?
- Approximately how many different contacts of this type have you had over this same two-year period?
- With whom were your (four most recent) contacts?
- Would you rate your contact with (1, 2, 3, 4) as being a positive, negative, or neutral experience? Why?

Community Interview, *supra* note 140, at 8-9, Nos. 16-16b, 16d.

151. The question asked was: "Could you please describe your contacts with (1, 2, 3, 4), including your intentions prior to the contact and the results of the contact?" *Id.* at 8, No. 16c.

opment strategies, and educates the community on how to purchase a house and how to avoid foreclosure.

Housing organizations have also used their analysis of the disclosure statements as an organizing tool in their neighborhoods. Residents of redlined areas are shown that their savings dollars are used to further investments in other neighborhoods rather than in their own. They are encouraged to protest discriminatory lending practices by depositing their money elsewhere. On occasion, other actions, including picketing, may be taken to attack the public relations image of a redlining lender. In those instances where it is possible to point out mortgage investment in the community, or when negotiations with lenders yield a positive result, the findings are used to promote confidence in neighborhood residents. They have also been used to support applications for community development block grant funds.¹⁵²

Some groups feel that several years of disclosure reports will be necessary to identify lending trends in the community they serve. In the meantime, they collect and analyze the reports in order to monitor lenders' compliance with the provisions of the HMDA. Several groups have written letters advising the Federal Home Loan Bank Board and the Federal Reserve of their findings.

C. *Financial Institutions' Use of Disclosure Data*

Two-thirds of the responding financial institutions, including both commercial banks and savings and loan associations, have analyzed their own disclosure reports.¹⁵³ Most used the data to determine their geographic loan distribution patterns.¹⁵⁴ Many found that loan investment is greatest around the institutions' branch offices.¹⁵⁵ Some institutions found that little money is invested in the inner city;¹⁵⁶ others found that too much is invested in "doubtful" areas.¹⁵⁷

152. The questions asked were the same as those asked concerning the findings of the housing organizations after they analyzed the disclosure statements. See notes 143 & 144 *supra*.

153. The questions asked were: "Has your institution analyzed the data from its own disclosure report? What were your findings? Did you use these findings for any specific purpose?" Financial Interview, *supra* note 144, at 7, Nos. 36-36b.

154. Seventy percent.

155. Twenty-three percent.

156. Eight percent.

157. Eight percent.

One-half of the group which analyzed their reports did not intend to use their findings for any specific purpose. Others indicated that the results would be used to increase their knowledge of where loans are being made, to pick new locations for branches, to talk to city governments, and to more actively encourage home loans in areas most in need of them.

Only one financial institution had collected disclosure reports from other lenders.¹⁵⁸ Another institution disclosed that savings and loan institutions had met and decided that "it would not be necessary to exchange reports—that would only waste paper." Several mentioned, however, that they had seen newspaper analyses of the disclosure data.¹⁵⁹

D. *Newspaper Analyses of Disclosure Data*

In January 1977, Thomas S. Andrzejewski authored a 2-day series of articles in the *Plain Dealer* analyzing the data obtained from financial institutions in Cuyahoga County under the HMDA.¹⁶⁰ The analysis entailed counting the number of houses (with four or less units) within each zip code zone from the 1974 Real Property Inventory. Areas of the county—inner city east, inner city west, inner ring, middle ring, and outer ring suburbs—were compared by the number of conventional mortgages per one hundred houses in each zip code zone. Four patterns emerged from this analysis. First, all white or mainly white sections of Cuyahoga County received a far greater proportion of conventional mortgages than did the black sections. Second, the suburbs averaged twice as many mortgages for every one hundred houses as the city and more than three times the mortgages granted on the predominantly black, east side of the city. Third, with the exception of two inner ring suburbs, lenders were making few conventional mortgages in integrated suburbs. Finally, there was little correlation between the percentage of mortgages in given areas of the city and the percentage of loan offices in those areas.

158. The questions asked were: "Has your institution obtained the disclosure reports of any other lenders? Has your institution analyzed the data from that report? What were your findings? Did you use these findings for any specific purpose?" Financial Interview, *supra* note 144, at 7, Nos. 37-37c.

159. See notes 160, 161 *infra* and accompanying text.

160. Andrzejewski, *Mortgageville's a Suburb*, *The Plain Dealer* (Cleveland), Jan. 2, 1977, § 2, at 1, col. 1.

Andrzejewski disclaimed any ability to prove or disprove red-lining or any other kind of mortgage discrimination with the information provided by the HMDA. His work did, however, substantiate the primary complaint of housing organizations throughout the county—that there is less conventional lending in the older, poorer, or integrated neighborhoods.

Financial institutions were uniformly aware of the *Plain Dealer* study, which included summaries of the lending data for ten commercial banks and thirty-four savings and loan associations. The lending institutions rebutted the findings of this study on the same grounds that they dismissed the analyses of the housing organizations—that “they can only make loans in neighborhoods where there are home sales and where prospective buyers apply for mortgages.”¹⁶¹ The newspaper analysis illuminated a second weakness of the HMDA: thorough analysis requires a great deal of time, access to skilled personnel, and sophisticated equipment. The research coordinator of the *Plain Dealer's* market research department began programming the computer and computerizing the data in October 1976. Three months of work produced hundreds of pages of computer printouts covering more than one billion dollars of loans. No housing organization in Cuyahoga County has resources to conduct a comprehensive mortgage analysis of this kind.¹⁶²

E. *Use of the Disclosure Data by Individuals*

Forty-two per cent of the residents of Cuyahoga County have heard of the HMDA according to the Cleveland Area Survey, conducted during the early months of 1977.¹⁶³ A little less than two per cent of those polled belong to organizations among whose goals is the prevention of housing discrimination.¹⁶⁴ Surpris-

161. *Id.* at col. 2.

162. *See* note 9 *supra*.

163. The question asked was: “Financial institutions like banks and savings and loans are now required by law to make available to the public, information about *where* they lend money for mortgage and home improvement loans, and *how much* money they lend. Are you aware of this law?” Staruch, *Sampling and Sample Characteristics—Cleveland Area Survey: 1976 and 1977 (1977)* (unpublished: available at Cleveland Area Survey, Department of Sociology, Case Western Reserve University). The Cleveland Area Survey was conducted within the three months following the *Plain Dealer* series on the HMDA.

164. The questions asked were: “Do you know of any groups around where you live that are organized to prevent discrimination against people who either want to improve their homes or buy homes around there? What are the names of these groups? Do you belong to any of these groups?” *Id.*

ingly, twice this number of people attempted to obtain copies of the disclosed reports. More than three percent succeeded in doing so. Of this latter group, twenty-eight percent actually used the reports in some way, and twenty percent anticipated using them in the future.¹⁶⁵

IV. WHAT MORE SHOULD BE DONE?

A. *Recommended Changes in the Home Mortgage Disclosure Act*

Redlining is a problem that causes deterioration of neighborhoods. It may occur because lenders fail to consider the social impact of the large number of discretionary choices made in the course of business. Because federally regulated financial institutions receive certain benefits from the government, they should be held accountable for their lending activities when these activities affect localized areas of the economy, such as housing in urban neighborhoods.¹⁶⁶

Congress has begun to deal specifically with redlining and its concomitant problems. The HMDA was a beginning, designed to set the background and provide information about the problem. But, as noted above, its use has been limited.¹⁶⁷ A comparison of the provisions of the Act with the mechanism of redlining reveals that the basic difficulty with the Act is that it does not provide enough information to prove that redlining exists. The Act requires that reporting institutions disclose their lending patterns, but the disclosure statements fail to reveal the number of applicants who were denied loans. The basic test for redlining must be a comparison between the number of loans requested and the number of loans made within each census tract.

The absence of information indicating loan demand is a major source of criticism by housing organizations in Cuyahoga County.¹⁶⁸ Not only did the organizations want the numbers of

165. The questions asked were: "Have you ever tried to get this information? (refers to questions on awareness of the HMDA). Did you get this information? What have you done or do you intend to do with this information?" *Id.*

166. See note 102 *supra* and accompanying text.

167. See notes 140-65 *supra* and accompanying text.

168. When asked an open-ended question of what changes should be made in the HMDA, 60% of the housing organizations suggested inclusion of loan demand information. Community Interview, *supra* note 140, at 16, No. 38a. When financial institutions were asked whether information about applications for mortgages should be included in the Act's reporting requirements, 17% replied affirmatively. Financial Interview, *supra*

refusals listed by areas, but they also suggested the need for information about the reasons for the refusal and the race and sex of the applicants. Such information would obviously be helpful in order to determine whether discrimination is occurring.¹⁶⁹

Of course, the process of considering an applicant for a loan is structured in such a way that an accurate count of applicants may be difficult to establish. Who is an applicant? The prospective buyer who is steered away from a particular neighborhood by a real estate broker who knows or thinks he knows banks will not lend there? The buyer who has found a home and is screened out by the loan officer before a formal application form is completed? The buyer who has paid an application fee but is refused by the loan officer after a credit check and property appraisal? The buyer whose application is refused by the loan committee? This problem is probably not insurmountable, however, in view of similar legislation dealing with credit application denials.¹⁷⁰

In order to detect redlining at its earlier stages,¹⁷¹ information in addition to that pertaining to loan refusals is necessary. The terms of mortgages granted should be spelled out, including interest rates, discount points and other fees, years until maturity, and percentage of downpayment required.

According to twenty percent of the housing organizations and seventeen percent of the financial institutions, the distribution of deposits of the financial institutions should also be shown by census tract. Disclosure of deposits was an original provision of the bill as introduced in committee,¹⁷² but it was subsequently removed before enactment. Opposition to the provision was based on a fear of credit allocation¹⁷³ and on the concern of financial

note 144, at 6, No. 33. Commentators on the Act also suggest the failure to provide loan demand information is one of its major drawbacks. See, e.g., Renne, *Eliminating Redlining by Judicial Action: Are Erasers Available?*, 29 VAND. L. REV. 987, 1004 (1976); Comment, *Red-Lining and the Home Mortgage Disclosure Act of 1975: A Decisive Step Toward Private Urban Redevelopment*, 25 EMORY L.J. 667, 697 (1976).

169. Thirty-five percent of the financial institutions agreed with the housing organizations that the race and sex of the borrower would be an appropriate subject for disclosure under the HMDA, Financial Interview, *supra* note 144, at 6, No. 33, but they were not asked whether that information should be available for loan applicants.

170. See The Equal Credit Opportunity Act, 15 U.S.C. § 1691 (1976). This Act is designed to ensure extension of credit "to all creditworthy customers" regardless of sex or marital status, and contains a definition of an "applicant." *Id.* § 1691a.

171. See notes 74-77 *supra* and accompanying text.

172. See *Hearings*, *supra* note 138, at 7.

173. See, e.g., *Minority Views on H.R. 10024, The Minority [sic] Disclosure Act of 1975*, H.R. REP. NO. 561, 94th Cong., 1st Sess. 32, reprinted in [1975] U.S. CODE CONG. & AD.

institutions that the publication of such information might weaken their competitive position relative to each other. Such a provision would measure the institutions' investment in the areas from which they derive their investment capital. In addition, disclosure of depository information would provide useful information for other aspects of regulation such as charter renewal or applications for branching.¹⁷⁴

The difficulty of obtaining and using the information reported by the HMDA limited the usefulness of the disclosure information to housing organizations in particular. Centralized collection and analysis of the data would be a reasonable method of making the information more accessible and usable. Centralization is not required by the Act or its regulations. In fact, the Federal Reserve Board has discounted recommendations for centralized data collection and analysis as contrary to the intent of the Act.¹⁷⁵ The Board reasoned that Congress had intended to avoid additional bureaucratic involvement by making the information directly available to private groups or individuals, so that the private bodies could take direct action. The Board failed to consider the relative ease with which statements could be compiled and analyzed, and the results disseminated by one agency among groups or individuals for free or at cost. In comparison, the present system in which an institution's disclosure statements are available only at the main office and one branch office of each institution causes individuals and groups to spend an inordinate amount of time duplicating each others' efforts to collect disclosure statements from all institutions in an area. Moreover, since the disclosure statements received are generally computer printouts, the information

NEWS 2326, 2327; Wisniewski, *Mortgage Redlining (Disinvestment): The Parameters of Federal, State, and Municipal Regulation*, 54 J. OF URB. L. 367, 378 (1977).

174. The Community Reinvestment Act of 1977, Pub. L. No. 95-128, tit. VIII, 91 Stat. 1147 (to be codified in 12 U.S.C. §§ 2901-2905) was enacted in October 1977 to "require each appropriate Federal financial supervisory agency to use its authority when examining financial institutions, to encourage such institutions to help meet the credit needs of the local communities in which they are chartered consistent with the safe and sound operation of such institutions." *Id.* § 2901(b). Depository information would be helpful in defining the community to which the institutions must be responsive.

175. Speaking on behalf of the Federal Reserve System, Theodore Allison stated: "The compilation of the information at the Federal level would not be in the spirit of the act because the Congress determined that local studies and solutions are the appropriate mechanism for dealing with local problems of disinvestment." Letter from Theodore E. Allison, Secretary, Board of Governors, Federal Reserve System, Washington, D.C., to David L. Hoehnen, Associate Director, Commission on Catholic Community Action, Cleveland, Ohio (Apr. 29, 1977).

is relatively difficult to decipher. Even when the information is comprehensible, the simple arithmetic comparisons needed for analysis are time consuming without access to computer time. When the time necessary to collect the statements is combined with the time required to do a simple comparative analysis between institutions, and this is multiplied by each individual or group who is interested in using the information, the costs in time alone make access to the information extremely expensive.¹⁷⁶ This does not even take into account the copying expenses that the institutions can pass on to those who use the disclosure statements.¹⁷⁷ It is apparent that tremendous disincentives are inherent in the Act and its regulations. These disincentives conflict with the express purpose of the Act and should be eliminated by centralizing collection and basic analysis within each area, and by making reports available to the public upon request.

Another weakness of the HMDA is that only depository institutions are required to report their lending activities.¹⁷⁸ These institutions conduct a large part of the residential mortgage lending in the country;¹⁷⁹ nevertheless, mortgage companies are unregulated by either the state or federal government and provide mortgages for many of the FHA insured home purchases. In fact, many of the accusations regarding abuse of the FHA program and other kinds of speculation are leveled at mortgage companies. As conventional lending becomes less available in an area, mortgage bankers become a more attractive source of funds when homes are bought and sold.¹⁸⁰ The HMDA should be amended to require any commercial lenders of residential mortgages to report.¹⁸¹

176. An additional time cost in the present study was incurred when a savings and loan company made "the materials available for copying," 12 C.F.R. § 203.5(c) (1977), by allowing anyone who wanted the information reported to copy it *by hand*. All other institutions made copies available.

177. The total amount paid to the 38 financial institutions surveyed for their disclosure reports was \$53.38. The cost per page ranged from zero to \$1.67. A copy of the disclosure statement of the institution referred to in note 176 *supra* was obtained from other sources.

178. See 12 U.S.C. §§ 2801, 2802(2), 2803 (1976).

179. See notes 26-29 *supra* and accompanying text.

180. See note 26 *supra* and accompanying text. Thus, the ratio between lending by mortgage companies and lending by conventional lenders is an excellent indicator of redlining.

181. Twenty percent of the housing organizations suggested, in open-ended answers to a question requesting recommended changes in the Act, that mortgage companies be included in the Act's reporting requirements. Community Interview, *supra* note 140, at 16, No. 33. Forty-eight percent of the financial institutions responded positively to the question whether mortgage bankers should be included. Financial Interview, *supra* note 144,

Despite the limitations of the HMDA, all the housing organizations and slightly more than one-half the financial institutions were opposed to permitting it to expire as it is scheduled to do in December 1979.¹⁸² All but two of the housing organizations indicated that it should be reenacted but with substantial changes. On the other hand, a quarter of the financial institutions suggested that it be reenacted as is, while another quarter suggested reenactment with substantial changes. The consensus of opinion is that the HMDA provides benefits which outweigh the costs of disclosure.

B. *Towards Preventing Redlining and Its Effects*

No one can argue that the HMDA is sufficient to eliminate the problems surrounding redlining. Housing organizations and financial institutions suggested numerous approaches to end redlining which are also discussed in the literature. The proposals seek either to return conventional financing to areas which have lost (or are losing) it or to alleviate the effects of loss of conventional financing. Combinations of these programs may temporarily alleviate the problem, and over the long run they may improve the investment environment sufficiently to bring back conventional financing. The programs generally focus on incentives or regulations to initiate reinvestment, or on the development of alternative financing by private organizations and public officials.

Broad agreement exists among the financial institutions and housing organizations surveyed that community groups play a vital role in encouraging reinvestment. When asked what is necessary to encourage investment, one-quarter of the financial institutions specifically suggested that neighborhood groups must provide the impetus to upgrade the quality of city neighbor-

at 6, No. 38a. They generally indicated that if depository institutions must report, so should nondepository mortgage companies.

182. 12 U.S.C. § 2809 (1976). The question asked of housing organizations and of financial institutions was: "Do you think that the Home Mortgage Disclosure Act of 1975 should a) be allowed to expire; b) be reenacted as is; or c) be substantially changed?" Community Interview, *supra* note 140, at 15, No. 38; Financial Interview, *supra* note 144, at 5, No. 29.

Housing organizations which wanted substantial changes were asked: "What should these changes be?" Community Interview, *supra* note 140, at 16, No. 38a. The changes suggested, in addition to those discussed in the text, were that a 2- or 3-year retroactivity of the disclosure requirement be implemented, that the data be more specific and standardized, and that financial institutions be required to divulge their full investment portfolios. The financial institutions were then asked their reactions to the housing organizations' recommendations.

hoods—by encouraging home improvements, building community pride, and negotiating with lenders.¹⁸³ Two institutions suggested an educational campaign to inform the public regarding the availability and processes of obtaining mortgages and the necessity for proper upkeep of the mortgaged premises. Presumably such an educational program could also be handled by community housing organizations, preferably in cooperation with city officials and financial institutions.

Housing organizations surveyed in this study also felt they had an important role to play in combating redlining by keeping the problem in the public eye.¹⁸⁴ They suggested putting pressure on financial institutions and on government to deal with the problems by “greenlining”¹⁸⁵—petitioning for city services, accumulating information on practices in the community, and communicating directly and through the media with financial institutions and governmental officials.

Government—at local, state, and national levels—is seen as an indispensable party in eliminating redlining. Control of financial institutions can be made more specific and enforced more vigorously through legislation, regulation, and governmental scrutiny.¹⁸⁶ Reorganizing or revamping federal governmental

183. The question asked was: “Assuming that one of the purposes of the HMDA is to encourage reinvestment in residential areas where loans have not been readily available, what suggestions would you have to accomplish that purpose?” Financial Interview, *supra* note 144, at 9, No. 45. Cooperative reinvestment programs were suggested by 14% of the financial institutions.

184. For a description of their activities, see notes 9 & 39 *supra* and accompanying text.

185. “Greenlining” is considered an antidote to redlining. Depositors withdraw their deposits from institutions that redline their community and redeposit their money in more responsive institutions.

186. Anti-redlining regulations by the Federal Home Loan Bank Board will provide much of this necessary governmental supervision. 43 Fed. Reg. 22,332 (1978) (to be codified as an amendment to 12 C.F.R. §§ 528, 531.8).

The regulations prohibit home loan denials, refusals to accept loan applications, or loan offers on less favorable terms because of the age of a dwelling or the neighborhood where it is located; they require written, nondiscriminatory underwriting standards and periodic review of advertising and marketing practices to assure that services of the lender are available to all segments of the community it serves; and the regulations prohibit discrimination in home lending on the basis of the applicant’s marital status, age, receipt of income from public assistance programs, or good faith exercise of rights under various consumer protection acts.

Speech by Donna Shalala, Assistant Secretary for Policy Development and Research, U.S. Department of Housing and Urban Development, at Housing and Community Development Conference, Case Western Reserve University School of Law (Mar. 4, 1978). See also the recommendations in Earthman, *Residential Mortgage Lending: Charting a Course Through the Regulatory Maze*, 29 VAND. L. REV. 957 (1976), and Wisniewski, *supra* note 173.

programs such as FHA insurance¹⁸⁷ and the secondary mortgage market¹⁸⁸ can enhance their constructive effect on neighborhoods. Local governments can improve essential services¹⁸⁹ and enforce housing codes.¹⁹⁰

Additional cooperation between government, financial institutions, and neighborhoods may enhance the chances for neighborhood revitalization. Affirmative investment programs, such as Neighborhood Housing Services,¹⁹¹ which require financial and governmental support in specific targeted neighborhoods, have been somewhat effective in slowing or reversing deterioration. Governmental requirements that financial institutions establish assigned-risk pools may provide mortgages to individuals for whom they would otherwise be unavailable.¹⁹²

Financial institutions remain the primary perpetrators of redlining. They must be encouraged or compelled to accept responsibility for the consequences of their lending choices. The latitude in their financial decisionmaking would permit them to avert discrimination and its effects. The HMDA can be useful in encouraging the accountability of financial institutions. The HMDA provides information that enables lenders to appreciate the cumulative effect of their individual decisions. The Act also provides information to private citizens, their organizations, and their representatives in government, making it possible for them to note lending patterns and confront financial institutions with their role in neighborhood change.

The HMDA is far from being a panacea. But it may crack the wall of "business necessity" which has shielded financial institutions from public accountability. And in so doing, it will perhaps

187. See Note, *Attacking the Urban Redlining Problem*, 56 B.U. L. REV. 989, 1014-16 (1976).

188. See Earthman, *supra* note 186.

189. This suggestion was mentioned by 14% of the financial institutions in response to the question quoted at note 183 *supra*.

190. This suggestion was mentioned by 17% of the financial institutions in response to the question quoted at note 183 *supra*.

191. For a description of Neighborhood Housing Services, see Duncan, Hood, & Neet, *Redlining Practices, Racial Resegregation, and Urban Decay: Neighborhood Housing Services as a Viable Alternative*, 7 URB. LAW. 510 (1975).

192. This suggestion was mentioned by 17% of the financial institutions. See also recommendations in Note, *supra* note 155, at 1016-18, on assigned-risk insurance pools.

begin the downfall of a destructive discriminatory structure and create in its place a cooperative financial structure.

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