NATIONAL COMMUNITY REINVESTMENT COALITION NCRC

Mortgage Lending Disparities Series Paper

Working-Class Families Arbitrarily Blocked from Accessing Credit

NCRC's Fair Lending Investigation of Credit Score Restrictions by Federal Housing Administration-approved Lenders

December 2010

Prepared by National Community Reinvestment Coalition

National Community Reinvestment Coalition

The National Community Reinvestment Coalition is an association of more than 600 community-based organizations that promote fair access to basic banking services, including credit and savings, and work to create and sustain affordable housing, job development, and vibrant communities for America's working families. Our members include community reinvestment organizations, community development corporations, local and state government agencies, faith-based institutions, community organizing and civil rights groups, minority- and women-owned business associations, and social service providers from across the nation. Their work serves primarily low- and moderate-income people and minorities.

The board of directors would like to express their appreciation to the NCRC professional staff who contributed to this publication and serve as a resource to all of us in the public and private sector who are committed to responsible lending:

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Introduction

When the mortgage finance and the housing market collapsed two years ago, private lenders reacted by tightening standards to the point of significantly constricting credit opportunities for many borrowers, even those with good credit. Out of necessity, the federal government remained one of the few sources of credit. This, along with other critical government actions, helped bring the economy back from the brink of total collapse.

However, while the Obama Administration has been successful at preventing a full blown economic depression, its ability to rebuild and strengthen the economy has been hampered by the continual refusal of financial institutions to lend to creditworthy individuals.

After years of what former Chairman of the Federal Reserve Board Alan Greenspan called "infectious greed," and "malfeasance," the financial industry continues to operate irresponsibly, pursuing arbitrary policies and practices that are detrimental to consumers and the economy.[1] Leading up to the economic crisis, many financial institutions pushed products that stripped consumers of their wealth, rather than building and improving their economic security or otherwise serving their financial interest.[2] During this time, mortgage lenders originated irresponsible, risky, and complicated financial products. This greed and malfeasance spread throughout the financial system and directly led to the foreclosure crisis, which continues to undermine the economy and destabilize tax bases in cities and states nationwide.

Today, these same lenders have swung the pendulum 180 degrees to a position that is also dangerous to the health of the economy. Large banks and independent mortgage companies are refusing to lend to a sizable segment of the population, disproportionately working-class families who have lower credit scores resulting from a temporary situation, such as job loss or an illness or other factors that do not accurately reflect an ongoing credit risk. This practice freezes efforts to revitalize the economy and to create jobs. Specifically, the nation's largest lenders have arbitrarily cut off access to one of the last remaining sources of credit: Federal Housing Administration (FHA) loans.

An investigation by the National Community Reinvestment Coalition (NCRC) discovered that a majority of the top 50 FHA lenders have instituted policies that limit access to credit to working families in low- and moderate-income communities, and in communities of color, the very same communities that have been most harmed by the greed and malfeasance of Wall Street and the financial industry. The investigation's findings were confirmed in consultation with FHA officials, best practice discussions with industry professionals, and by NCRC's work directly with consumers and our member organizations around the country.

NCRC's investigation reveals that too many of the country's largest financial institutions are refusing to lend under the FHA loan program to consumers with credit scores between 580 and 640, despite the fact that FHA policy establishes a 100% guarantee for refinance and home purchase loans to a credit score of 580 for borrowers with a 3.5% downpayment. Our

[1] http://www.federalreserve.gov/boarddocs/hh/2002/july/testimony.htm
[2] http://abcnews.go.com/Business/story?id=87049&page=1

investigations shows the majority of top lenders have minimum credit score requirements of 620 or 640.

These across-the-board restrictions have no legitimate business defense, since these loans are 100% guaranteed against losses except in cases where the lender fraudulently or improperly originated the loan. Importantly, FHA has put into place more stringent lending standards to ensure that taxpayers are not on the hook for losses.

NCRC calls on the U.S. Departments of Justice and Housing and Urban Development, the Federal Reserve, the Federal Deposit Insurance Corporation, the Office of Thrift Supervision, and the Office of the Comptroller of the Currency and the Consumer Financial Protection Bureau to investigate and end these practices[3]. In addition, NCRC calls on our nation's lenders to voluntarily revise their policies and to extend credit, in a safe and sound manner, to all hardworking Americans based on their ability to pay and other strong underwriting standards. Doing so will not only help strengthen our economic recovery, but will ensure that all Americans, regardless of race, are able to access credit and the window to prosperity it can provide.

This widespread policy has profound consequences for consumers, their families, and the economy. Nearly one-third of all Americans have credit scores below 620, thus, a significant segment of the American public is being denied access to credit. To make matters worse, NCRC has discovered that many lenders are moving to increase their minimum credit score requirements. This would deny credit opportunities to millions of potential homeowners.[4]

Not only do these policies deny access to credit to qualified individuals seeking to purchase or refinance a home under the FHA loan program, but they are also restricting the availability of credit and the ability of the economy to recover. Today, FHA is one of the only avenues available to Americans seeking to purchase or refinance their homes. Because the program relies on private lenders to originate the mortgage, the lenders are serving as gatekeepers. To arbitrarily deny nearly a third of Americans this remaining source of credit poses a great threat to the nation's economic recovery.

Ultimately, these policies are in contradiction of the purpose and intent of the FHA loan program, which was created during the Great Depression to help working class Americans secure access to credit in order to realize or sustain homeownership at a time when the private lending market was nearly frozen.

In the past two years, FHA has continued to serve its vital counter-cyclical role, preserving and promoting economic stability and growth, at a time when private lending has otherwise been extremely limited. The financial crisis crisis sharply curtailed the flow of private sector loans to the point where FHA and the Government-Sponsored Enterprises (GSE) owned or guaranteed

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[4] http://www.bloomberg.com/news/2010-11-17/home-ownership-gets-harder-for-americans-as-lenders-restrict-fha-mortgages.html

nearly 95 percent of the new mortgage loans being originated.[5] By the end of 2008, almost one half of the home purchase loans and one quarter of the refinance loans were FHA or Veterans Affairs (VA) insured.[6]

In addition to stunting our economic recovery, this policy has a disproportionate and adverse impact on African-American and Latino individuals, families, and communities. Recent Home Mortgage Disclosure Act (HMDA) data, private sector data, and federal agency reports clearly demonstrate the significant role FHA has played in originated loans to minority consumers. By denying access to FHA loans to qualified, creditworthy individuals, without justification for the actual risk posed to the financial institution, lenders are discouraging the flow of credit and capital into communities of color. These policies amount to discrimination in violation of the Fair Housing Act, the Equal Credit Opportunity Act, and the Community Reinvestment Act.

NCRC's Expertise

With a membership of more than 600 community-based organizations, NCRC promotes fair access to basic banking services, including credit and savings, and to create and sustain affordable housing, job development, and vibrant communities for America's working families. NCRC is firmly committed to increasing fair and equal access to credit, capital, and banking services and products for all Americans, regardless of race, color, religion, national origin, gender, familial status, disability or age. NCRC is also a United States Department of Housing and Urban Development (HUD) certified "Qualified Fair Housing Enforcement Organization" and "National Housing Counseling Intermediary."

Our National Neighbors program is composed of civil rights experts with decades of experience with fair lending and fair housing issues, and is nationally recognized as an expert on testing methodology. Over the past decade, NCRC has conducted thousands of fair lending tests, commonly referred to as mystery shopping, across the nation on a wide range of subjects. Compliance audits have included testing financial service companies, regional and national banks, mortgage bankers and brokers, real estate offices, for-profit foreclosure prevention service providers, and payday lenders.

Investigation Findings

For this investigation, NCRC sought to determine if the nation's largest FHA lenders have instituted arbitrary and restrictive policies and practices, and whether these policies have an adverse and disparate impact on African-American and Latino consumers. Lenders were chosen according to their market share and volume of FHA loans, as well as through discussions with community leaders. While NCRC is continuing its investigation of FHA-approved lenders, the initial results as of December 8, 2010 were staggering. A list of the FHA-approved lenders that

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[5] http://www.frbsf.org/publications/economics/letter/2009/el2009-33.html

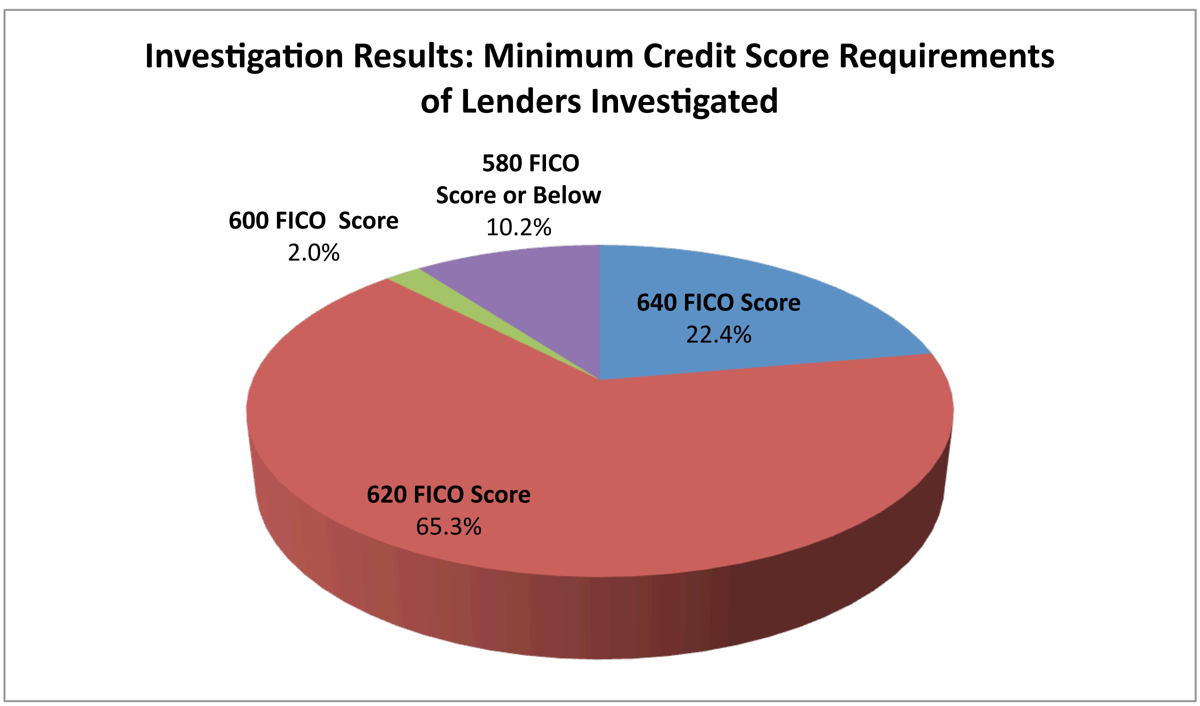
[6] Robert B. Avery, Neil Bhutta, Kenneth P. Brevoort, Glenn B. Canner, Christa N. Gibbs, *The 2008 HMDA Data*
The Mortgage Market during a Turbulent Year, in the Federal Reserve Board Bulletin, September 30, 2009, p. 20, see http://www.federalreserve.gov/pubs/bulletin/2009/pdf/hmda08draft.pdf.

NCRC is filing complaints against as of December 8, 2010, is included as Appendix A. Other investigations are ongoing.

NCRC utilized the technique of fair lending “testing,” or “mystery shopping,” to investigate the mortgage lenders practices. Our testers represented that they were interested in obtaining a home loan and that they had FICO scores at differing levels between 580 and 619. Testers were not seeking an FHA Streamline product (which refinances existing FHA loans) or other boutique products. If a lender stated that they could not originate a loan, the tester was instructed to ask about the FHA loan program and why the lenders policies were different than FHA’s. In order to illustrate the experiences of our mystery shoppers, a set of vignettes are included in this report under Appendix B.

Our mystery shoppers’ experiences were verified in consultation with FHA officials, best practice discussions with industry professionals, and by NCRC’s work directly with consumers and our member organizations around the country.

Of all the lenders tested, 44 did not lend at a 580 credit score. Thirty two lenders, or 65 percent, refused to lend to consumers with credit scores below 620. An additional 11 lenders, or 22 percent, refused to extend credit to consumers with credit scores below 640. One lender refused to lend to consumers with credit scores below 600. Only 5 lenders, or 10 percent, had policies in place that served the needs of consumers with credit scores between 580 and 620, in accordance with FHA policy and in compliance with fair lending laws. These findings are likely to become more pronounced, since many lenders have recently indicated that they intend to raise their minimum credit score requirements even higher.



The total number of lenders investigated who do not make FHA loans at a 580 credit score represent roughly 67 percent of the entire FHA market share, leaving many consumers without any other alternative to access credit. When this many FHA-approved lenders impose an arbitrary restriction on credit, millions of Americans are affected. This includes consumers seeking to purchase a home, as well as those whose homes have been sitting on the market without a buyer able to obtain a loan. In the end, these policies stunt the ability of the housing market to return to normal levels and they prolong the effects of the recession.

These policies have a particularly devastating impact on low- and moderate-income communities and communities of color by constricting their ability to access credit. These communities are experiencing "double jeopardy," having first been targeted for risky, toxic loans that lead to a tsunami of home foreclosures still sweeping across the nation, they are now being denied the opportunity to access one of the few currently available mortgage products, frustrating their ability to rebuild, protect or grow their wealth through a refinance or a home purchase with a responsible loan product.

NCRC has begun filing complaints with the Department of Housing and Urban Development (HUD) seeking an end to these arbitrary and restrictive minimum credit score requirements. Not only do these policies contradict established FHA policy, but they also unduly restrict access to credit and have an adverse and disparate impact on African American and Latino borrowers, in violation of the Fair Housing Act, for which HUD has jurisdiction. NCRC has also asked other regulators to investigate possible violations of the Equal Credit Opportunity Act, and the Community Reinvestment Act[7].

Arbitrary Decisions Are Not Good Business

The findings of our investigation have devastating ramifications for consumers, their families and communities, and the economy. Mortgage rates are at an all-time low, but homebuyers cannot access credit and homeowners cannot refinance.

While investigating the practices of FHA-approved lenders, NCRC encountered hollow justifications from lenders as to why they choose not to lend to borrowers with credit scores below 620. The justifications offered did not document actual risk to the financial institution if they originated loans in a safe and sound manner. These business defenses also do not justify the disproportionate and adverse impact these policies have on African-American and Latino borrowers and communities. What follows is a review of some of the most common justifications rebutted:

Lenders Are Not Assuming the Credit Risk, They Are Only At Risk For Their Own Underwriting Failures

Lenders claim that they are unable to originate loans in full compliance with FHA policy because originators face a substantial risk of liability for the indemnification of loans within the FHA loan program and that this risk is particularly high for loans originated to consumers with credit scores between 580 and 620. However, both originators and investors have a 100 percent loan guarantee from the FHA for all responsibly and appropriately underwritten loans. Originators are only at risk for their own underwriting errors, a clause that has always been a requirement in the secondary market. The risk to the originator is the same regardless of the FICO score.

The FHA has also recently tightened its underwriting requirements to ensure that only sustainable loans are insured and has further reported to Congress that the entire portfolio is performing well, including loans originated for consumers with credit scores between 580 and 620.

Lending to Consumers With 580-620 Credit Scores Won't Spike Foreclosures and Lead to More Losses

Some lenders argue that consumers with credit scores between 580 and 620 are not qualified to own a home and are a bad risk. As noted above, the risk is not born by the lender unless the loan was fraudulently or improperly originated. Further, FHA loan products are only originated to qualified consumers who meet all of the program's safety and soundness and responsible loan underwriting standards. FHA loans do not contain the layering of risky attributes, such as loans with low-documentation, balloon payments, or pay-option Adjustable Rate Mortgages (ARMs) that contributed to high delinquency rates among subprime loans at the height of the boom.

Income is also not a significant factor in loan performance. In meetings between NCRC and FHA, officials have said that low- and moderate-income tranches of FHA loans are performing as well or better than other portions of the FHA portfolio.

While it is true that in 2007 and 2008 the FHA loan program was plagued with problems that ultimately affected the performance of the entire portfolio, the current leadership at FHA has reformed the program and it is performing admirably at a time of critical need. Stronger underwriting and credit requirements, including a requirement for 10 percent down payments for consumers who have credit scores of 579 or below, has minimized this risk. FHA has also taken drastic steps to increase enforcement actions against lenders that fraudulently or irresponsibly originated loans in years past, which contributed to a higher rate of delinquency; FHA suspended some lenders, and withdrew approval for over 1,500 lenders. They also levied $4.27 million in penalties against non-compliant lenders.[8]

The changes are working. FHA has reported significant reductions in serious delinquency rates and actual claim payments. An independent actuary lowered the estimate of actual claims against FHA by $3.7 billion following these reforms.

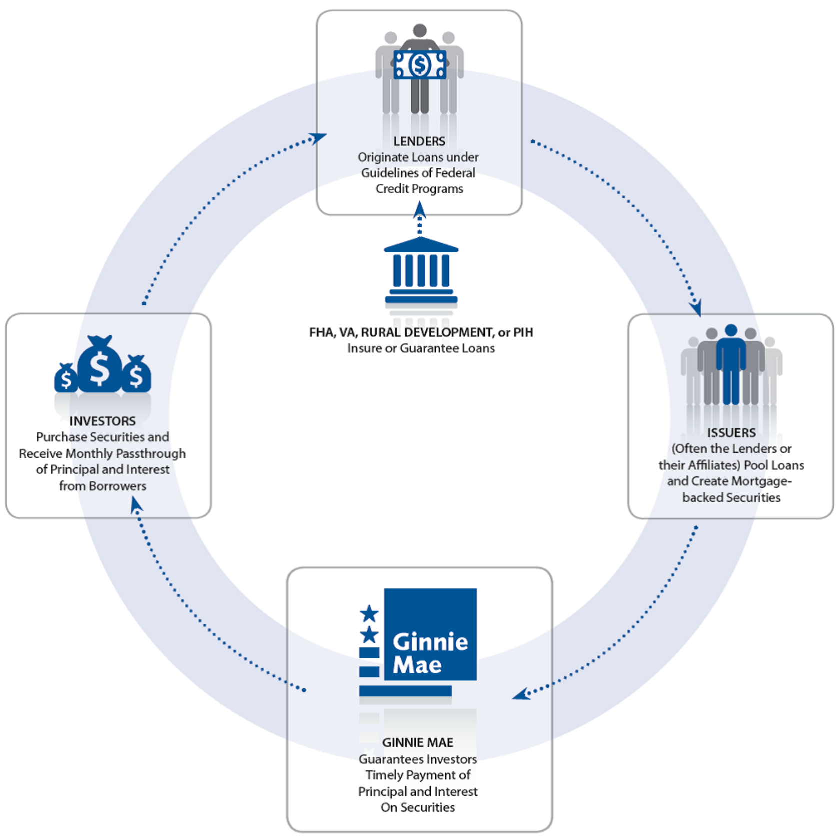
Today, nearly one-third of all Americans have a credit score below 620. While some of these consumers may not, in fact, be creditworthy, many more have experienced declines in their

[8] Testimony of FHA Commissioner David Stevens, Hearing before the House of Representatives Committee on Financial Services Wednesday, September 22, 2010

credit score due to a temporary bout of unemployment, restriction of their credit card limits, or other factors related to the credit crisis and the recession, or otherwise through no fault of their own. Other consumers were unable to remain current on risky and unsustainable loans offered by unscrupulous lenders; these loans should have never been originated in the first place. These hard working families are being locked out of a refinance or home purchase loan inappropriately, further delaying the economic recovery.

You Can't Blame it on the Secondary Market

Some lenders argued that they would be unable to sell FHA loans on the secondary market. However, FHA loan products are commonly sold to the secondary market. Ginnie Mae, a Government Sponsored Enterprise (GSE) within the U.S. Department of Housing and Urban Development (HUD), insures, securitizes, and then sells FHA loans on behalf of FHA approved lenders. The lenders we investigated could meet a variety of credit needs, especially those of first-time homebuyers, African-American and Latino consumers, and low- and moderate- income borrowers, by selling using Ginnie Mae, which sells high volumes of FHA loans to private sector investors. Many of the lenders included in NCRC's investigation are Ginnie Mae-approved originators.[9]



Source: Ginnie Mae FY 2010 Report to Congress

[9] http://www.ginniemae.gov/issuers/sf_issuers.pdf

Ginnie Mae does not consider credit scores when bundling loans. Investments in Ginnie Mae securities are among the safest on the market, and carry the full faith and credit of the United States.

Many lenders also claim that their hands are tied because Wall Street investors or the other Government Sponsored Enterprises (GSEs) will not buy the loans that they originate. If Wall Street firms or the other GSEs refuse to package or securitize these loans because they too implement a minimum credit score, then they are also in violation of the Fair Housing Act and related civil rights laws. This is nothing less then a new form of redlining, which promotes disinvestment at a time when access to credit is critical.

Lenders Cannot Use Credit Overlays In Violation of Fair Housing Law

Lenders also claim that they have the authority to use their own credit score minimum requirements, or "credit overlays." FHA-approved lenders have only limited discretion to do so in order to address actual risk documented within their portfolio. Lenders may not establish pricing or credit overlay policies that violate the Federal Fair Housing Act or the Equal Credit Opportunity Act.

NCRC acknowledges that specific FHA portfolios and channels perform differently. Our focus for this investigation was on the traditional FHA mortgage and refinance products, and not the FHA Streamline program, which refinances existing FHA loans. Loans originated by brokers and in particular geographic regions may have unique characteristics. But these factors should not limit access to credit to responsible and qualified applicants broadly; across the board FICO restrictions exclude qualified borrowers and violate the law.

In sum, these arguments do not justify the disproportionate, and adverse, impact these policies have on African-American and Latino individuals, families, and communities. These policies amount to discrimination in violation of the federal Fair Housing Act, the Equal Credit Opportunity Act, and the Community Reinvestment Act.

The Restrictions Are Not Good Business

Lenders claim that the tightening of mortgage accessibility is directly related to the financial crisis. They claim that because of our country's weakened economic state, lenders are unable to extend credit. However, through our fair lending testing, NCRC identified a number of responsible lenders who are originating loans in compliance with the full breadth of the FHA policy, including qualified consumers with credit scores of 580 and above. These companies have found the program to be profitable and have readily sold their loans in the secondary market.

Numerous industry leaders have raised concerns about the availability of credit and its vital role restoring stability and growth to the economy. According to the National Association of Realtors (NAR), the availability of credit across a wide breadth of the population is one of the most important factors in a housing recovery. Lawrence Yun, Chief Economist at NAR argues that "modest changes in mortgage rates are less important to a housing market recovery than the number of people who are able to obtain mortgages.[10]"

Public sector leaders, including Sheila Bair, Chairman of the Federal Deposit Insurance Company, have warned that limiting the accessibility of credit can uproot the gains the economy has experienced. Noting that in 2009 banks registered the steepest decline in lending over the last 67 years, Ms. Bair warned that excessively tight credit could hinder our national recovery.[11] She questioned the reasons for the restriction: "A light needs to be shined on this and explanations need to be made where credit is not being provided."

Former Treasury Secretary Henry Paulson argued that the Troubled Asset Relief Program (TARP) program was necessary to avoid credit constriction. Paulson warned against "frozen credit markets that threaten American families' financial well-being, the viability of businesses both small and large, and the very health of the economy."[12] According to Paulson, TARP was intended to avoid the proliferation of toxic mortgage-related assets that were "choking off the flow of credit which is so vitally important to the economy. We must address this underlying problem, and restore confidence in our financial markets and financial institutions so they can perform their mission of supporting future prosperity and growth." Yet, while TARP and other government interventions were ultimately successful in preventing a total collapse of the economy, more than two years later, the very same banks that received this unprecedented government bailout are still not lending.

The Increased Role of FHA Lending In Our Communities

The Federal Housing Administration (FHA) was created in 1934 to serve an important counter-cyclical role in our nation's housing market. After housing prices had crashed during the Great Depression, the FHA helped keep the mortgage market afloat by providing affordable housing options when the private financial industry would not. Today, the FHA continues to serve this counter-cyclical role. When the hobbled private sector reduced its lending in 2008 and 2009, the FHA increased its presence in the market to provide sustainable homeownership loans and refinance options to help borrowers refinance out of the exotic, risky and expensive loans of the boom years into affordable, standard fixed-rate mortgages.

Prior to the recent financial crisis, FHA lending constituted less than 3 percent of the housing market. However, when credit markets froze in 2008, the FHA filled the void, "insuring approximately 30 percent of purchases and 20 percent of refinances in the housing market. Since January 2009, the agency has helped nearly 3 million Americans either purchase a home, or refinance into more stable, affordable mortgages," according to the Department of Housing and Urban Development (HUD), FHA's parent agency.[13] When HUD released its annual report to Congress, FHA loans accounted for nearly 40 percent of all purchase mortgages, for the period

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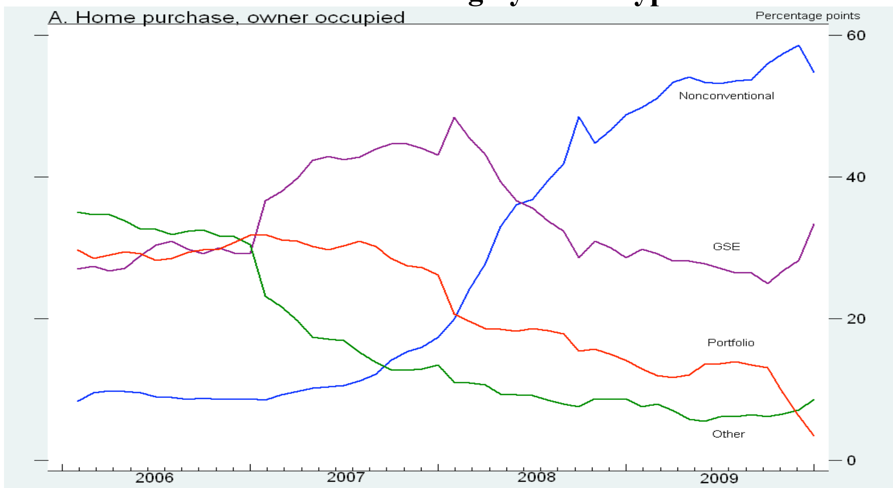
[10] http://www.theepochtimes.com/n2/content/view/46136/
[11] http://abcnews.go.com/Business/fdic-chief-banks-raise-lending-urges-public-pressure/story?id=10042775
[12] http://www.treas.gov/press/releases/hp1153.htm
[13] http://portal.hud.gov/portal/page/portal/HUD/press/testimonies/2010/2010-09-22

of November 2009 to November 2010.[14] Overall, government-backed loans -- which include FHA, Veterans Affairs (VA), and loans backed by the GSEs -- accounted for 38 percent of home purchase loans in 2006, but rose to nearly 82 percent by 2009.

Meanwhile, government-backed (government-insured or backed by the GSEs) refinance lending surged from 27 percent of loans in 2006 to 76 percent in 2009, while the share of non-conventional (or just government-insured) loans grew from 3 percent to 19 percent over the same time period.

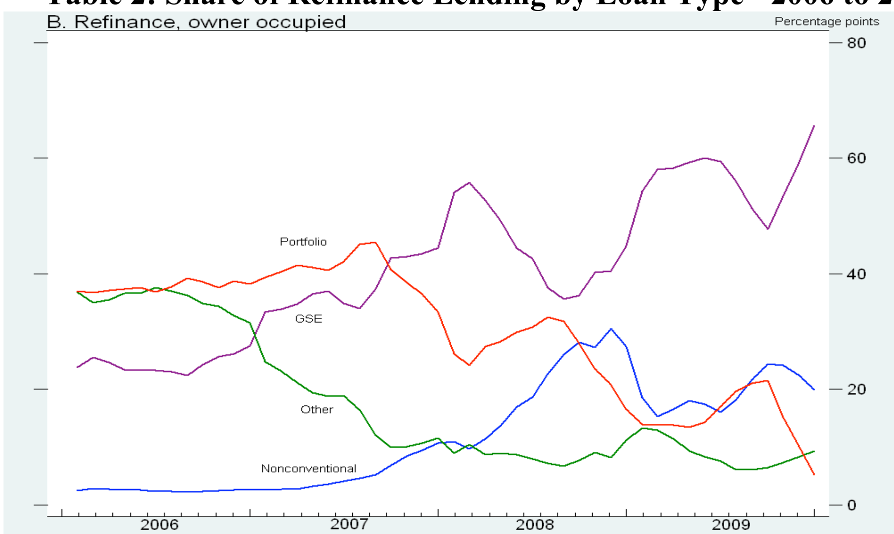
[14] http://www.homebuyinginstitute.com/news/fha-market-share-102/

Table 1: Home Purchase Lending by Loan Type - 2006 to 2009



Source: Federal Reserve

Table 2: Share of Refinance Lending by Loan Type - 2006 to 2009

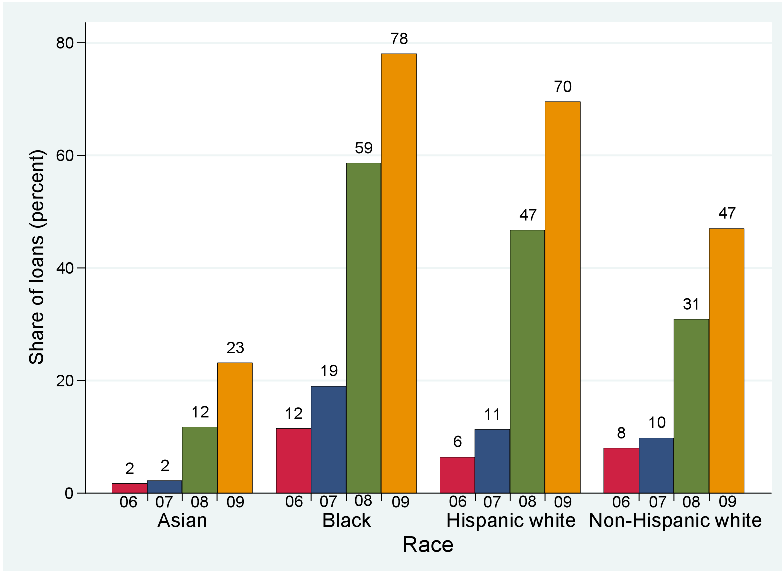


Source: Federal Reserve

According to the Federal Reserve, the principal reason why FHA's share of the market has increased so dramatically is because borrowers have fewer options since the private sector, including lenders and private mortgage insurance companies, reduced acceptable loan-to-value ratios and raised minimum credit score requirements.

While FHA lending goes to Americans of all demographics, it is one of the most vital tools available for helping low- and moderate-income and minority families purchase homes. Among homebuyers, low-income individuals and African-American and Latino homeowners use nonconventional loans to a much greater extent than their white counterparts. For example, in 2009, 78 percent of home purchase loans taken out by African-American homeowners were nonconventional, compared to 47 percent for white consumers (See Table 3 below).

Table 3: Incidence of Nonconventional Loan Originations by Borrower Race 2006 -2009



Source: Federal Reserve

Roughly 64 percent and 65 percent of the home purchase loans issued in low- and moderate-income tracts and to low- and moderate-income borrowers, respectively, were government-insured in 2009.[15] The table below (see Table 4) demonstrates that low- and moderate-income consumers turned to nonconventional loans in large numbers.

When lending institutions refuse to offer government-insured loans to borrowers with credit scores at or above 580, they are neglecting their Community Reinvestment Act (CRA) obligation to affirmatively serve all communities, including low- and moderate-income communities, consistent with safe and sound operations. HUD has determined that responsibly underwritten FHA loans can be made to low- to moderate-income borrowers in the 580-640 credit score range. Cutting off these modest income borrowers credit score range violates CRA's affirmative mandate to serve communities.

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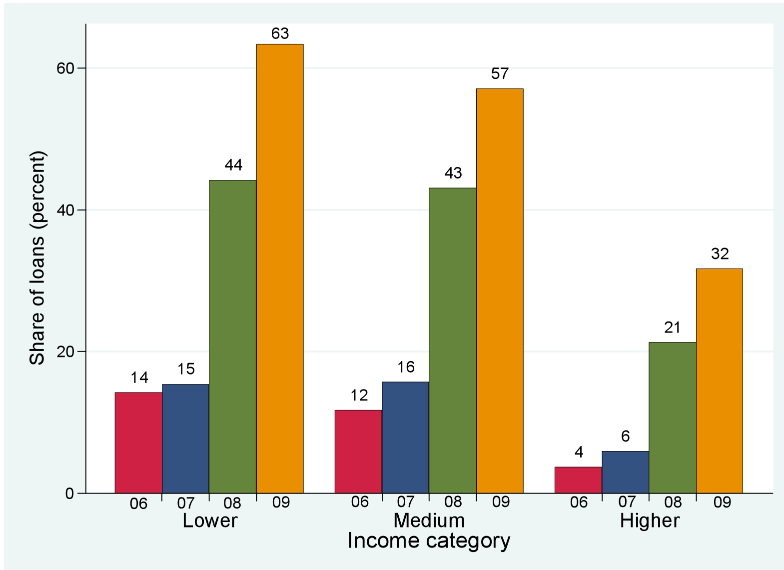
[15] Robert B. Avery, Neil Bhutta, Kenneth P. Brevoort, and Glenn B. Canner, *The 2009 HMDA Data: The Mortgage Market in a Time of Low Interest Rates and Economic Distress*, in the Federal Reserve Bulletin, September 2010.

Table 4: Incidence of Nonconventional Loan Originations by Income Level 2006 to 2009



Source: Federal Reserve

Analysis of Credit Scores by Race of Neighborhood Reveals Disparate Impact of Policies

An analysis of FHA loans conducted by NCRC using the Lender Processing Services (LPS)[16] database reveals that these loans disproportionately serve borrowers with credit scores between 580 and 620. In addition, our analysis finds that zip codes with concentrations of minorities contain a disproportionate percentage of consumers with FICO scores between 580 and 620. Therefore, financial institutions that adopt policies of not offering FHA loans to borrowers with credit scores between 580 and 620 will disproportionately and adversely affect access to FHA loans for predominantly minority neighborhoods.

According to the LPS dataset for home purchase loans originated in 2008 to owner-occupants, 18.4 percent of the borrowers for FHA loans had FICO scores between 580 and 620. In contrast, only 1.5 percent of the conventional loans were offered to borrowers with FICO scores between 580 and 620, see Table 5.

[16] LPS or Lender Processing Services is compiled from 16 mortgage servicing firms, including nine of the top ten servicers in the United States. The data does not capture all loans issued in the United States but is a large sample which is widely used in research. For additional discussion of the LPS dataset, see Dan Immergluck, Intrametropolitan Patterns of Foreclosed Homes: Zip-Code Level Distributions of Real-Estate-Owned (REO) Properties during the U.S. Mortgage Crisis, published by the Federal Reserve Bank of Atlanta, Community Affairs Discussion Paper, No. 01-09, April 21, 2009.

Table 5: Loan Type

Credit Score 581-620	**Percent**	**Number***
FHA Residential Loans	18.5%	49,715
Conventional Loans w/o PMI	1.54%	4,101
Conventional Loans w/ PMI	1.45%	2,629

(*Number is count of loans received by borrowers with FICO scores between 580 and 620.)

Since FHA is a market niche for borrowers with FICO scores between 580 and 620, a disparate impact - in violation of federal fair housing law - occurs if financial institutions do not adopt FHA's policy of offering FHA loans to borrowers with credit scores of 580 and above. The LPS data show that a disproportionate portion of individuals residing in predominantly minority zip codes have FICO scores between 580 and 620. While approximately 8 percent of individuals in zip codes with at least 80 percent of white residents have FICO scores between 580 and 620, more than 17 percent and 9 percent of individuals in zip codes with at least 50 percent African Americans and Hispanics, respectively, have FICO scores in that range, as illustrated in Table 6 and Chart 1.

The disparity is larger when considering only borrowers of FHA loans originated during 2008. About 28 percent of borrowers in predominantly African-American zip codes have FICO scores between 580 and 620 compared to just 18 percent of borrowers in white zip codes (see Chart 2, Tables 7a and 7b, pp. 17-18).

Table 6: Distribution of all home loans within credit score ranges by zip code racial composition

	50% or greater Hispanics	50% or greater African Americans	80% or greater Whites
Less than 580	2.89%	5.97%	2.47%
580 - 620	9.19%	17.34%	7.59%
Greater than 620	87.93%	76.69%	89.94%

Chart 1: Distribution of all home loans within credit score ranges by zip code racial composition

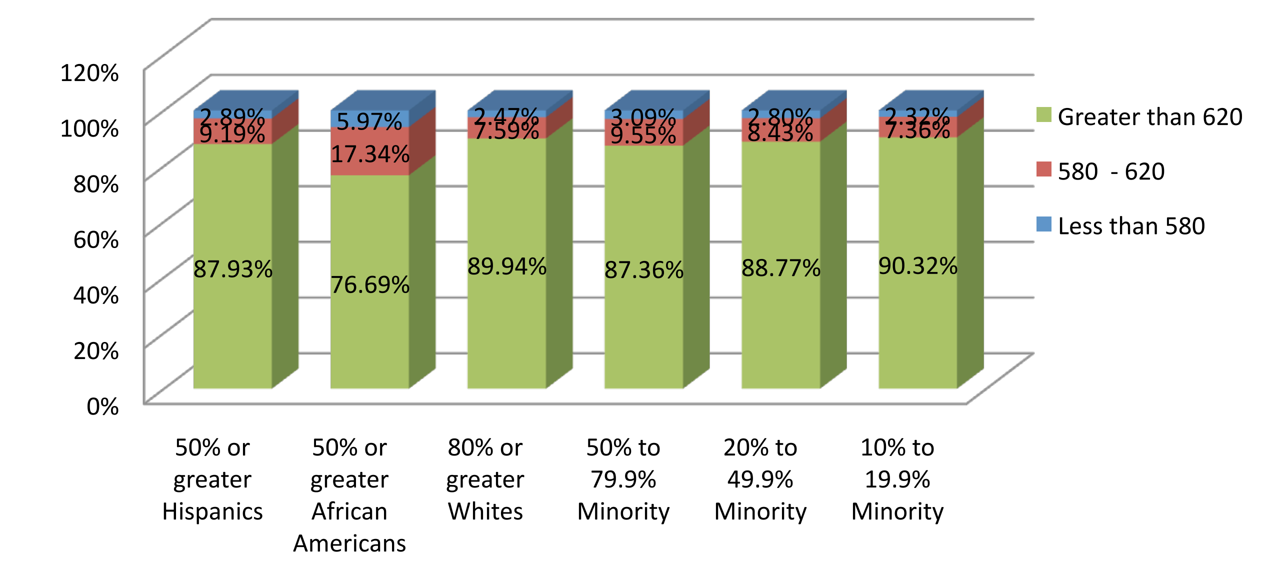


Chart 2: Distribution of FHA residential loans within credit score ranges by zip code racial composition

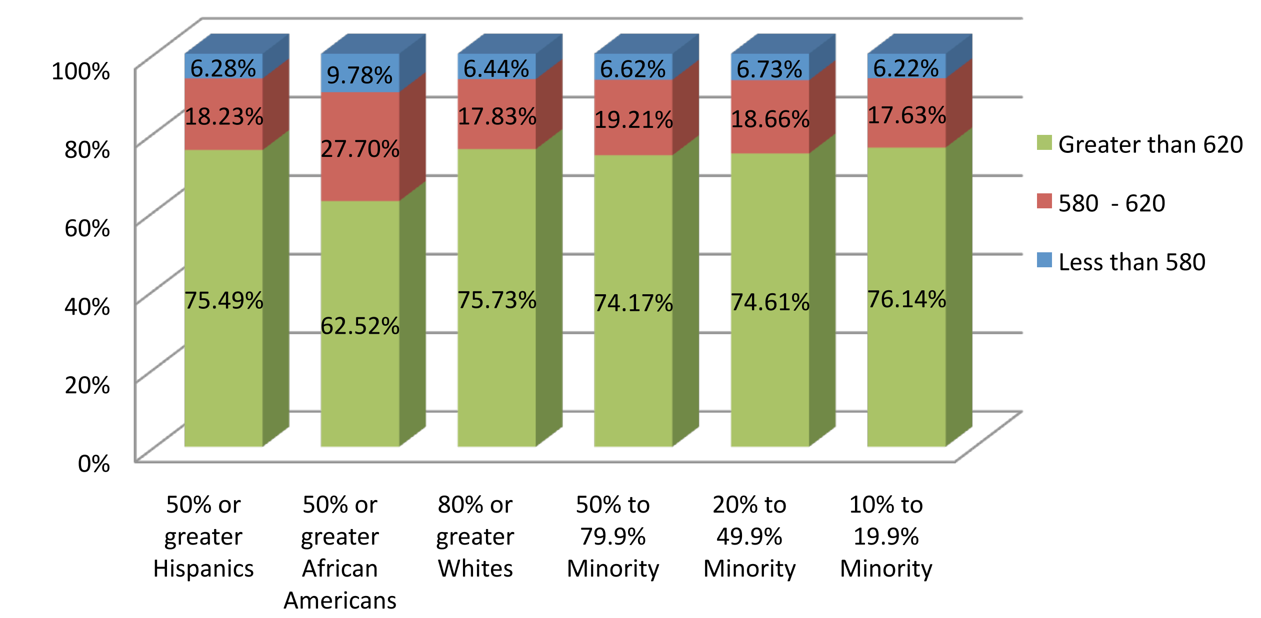


Table 7a: Number of FHA residential loans within credit score ranges by zip code racial composition			
	50% or greater Hispanics	50% or greater African Americans	80% or greater Whites
Less than 580	923	1,124	8,615
580 - 620	2,678	3,185	23,835
Greater than 620	11,092	7,189	101,238
Total	14,693	11,498	133,688

Table 7b: Distribution of FHA residential loans within credit score ranges by zip code racial composition			
	50% or greater Hispanics	50% or greater African Americans	80% or greater Whites
Less than 580	6.28%	9.78%	6.44%
580 - 620	18.23%	27.70%	17.83%
Greater than 620	75.49%	62.52%	75.73%

The percentage of borrowers with FICO scores between 580 and 620 is considerably lower when considering borrowers of conventional loans with and without private mortgage insurance (see Chart 3 and 4, Tables 8a, 8b, 9a, and 9b, pp. 19-21). This reinforces the conclusion that FHA has a particular market niche for consumers with FICO scores between 580 and 620, meaning that any policy that excludes borrowers with scores in this range will disproportionately impact minorities.

Chart 3: Distribution of conventional private mortgage insurance loans within credit score ranges by zip code racial composition

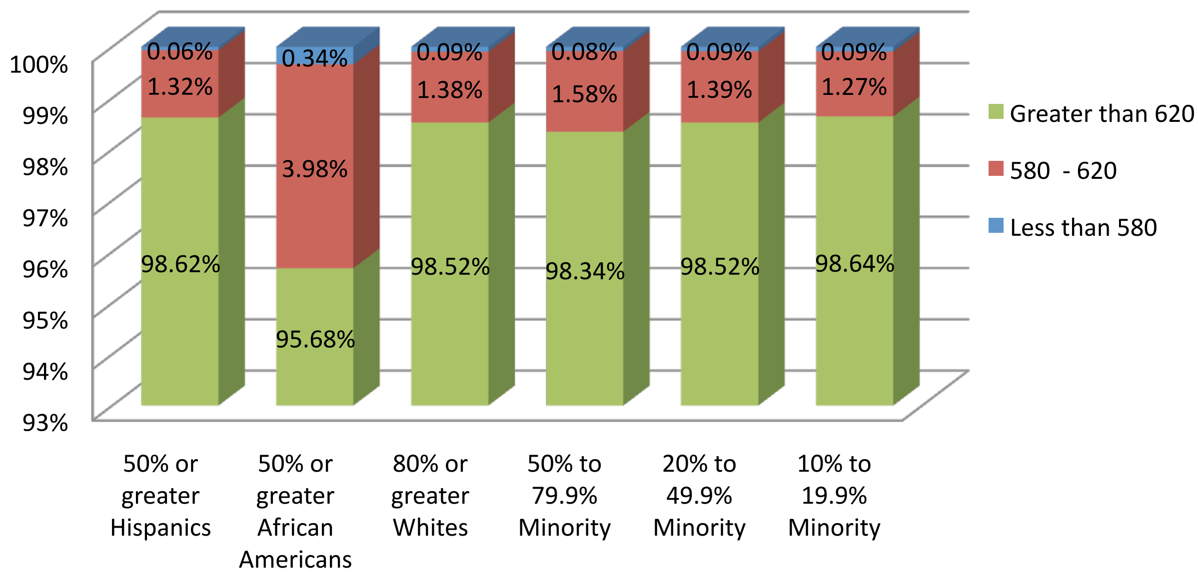
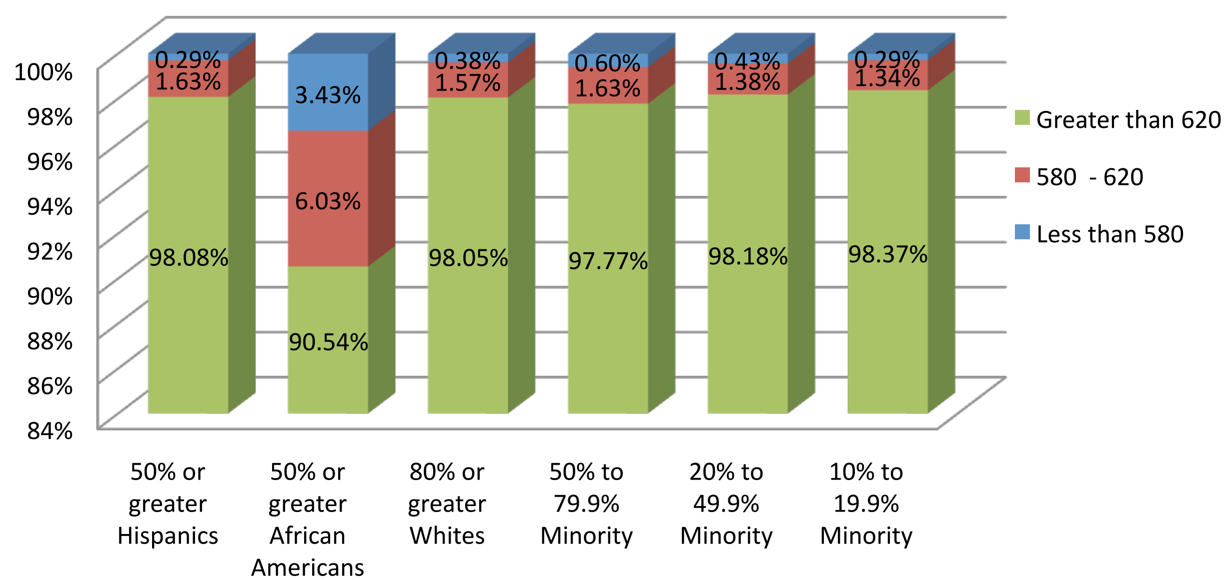


Chart 4: Distribution of conventional (without private mortgage insurance) loans within credit score ranges by zip code racial composition



	50% or greater Hispanics	50% or greater African Americans	80% or greater Whites
Less than 580	6	19	92
580 - 620	122	221	1,347
Greater than 620	9,143	5,314	95,875
Total	9,271	5,554	97,314

Table 8b: Distribution of conventional private mortgage insurance loans within credit score ranges by zip code racial composition			
	50% or greater Hispanics	50% or greater African Americans	80% or greater Whites
Less than 580	0.06%	0.34%	0.09%
580 - 620	1.32%	3.98%	1.38%
Greater than 620	98.62%	95.68%	98.52%

Table 9a: Number of conventional (without private mortgage insurance) loans within credit score ranges by zip code racial composition			
	50% or greater Hispanics	50% or greater African Americans	80% or greater Whites
Less than 580	27	144	548
580 - 620	150	253	2,272
Greater than 620	9,022	3,798	141,634
Total	9,199	4,195	144,454

Table 9b: Distribution of conventional (without private mortgage insurance) loans within credit score ranges by zip code racial composition			
	50% or greater Hispanics	50% or greater African Americans	80% or greater Whites
Less than 580	0.29%	3.43%	0.38%
580 - 620	1.63%	6.03%	1.57%
Greater than 620	98.08%	90.54%	98.05%

NCRC's findings corroborate the recent report of the Woodstock Institute (an NCRC member), which found that minority neighborhoods likewise had a disproportionate number of individuals with FICO scores below 620 in Illinois.[17] And the refusal of lenders to loan to all qualified FHA borrowers, has had an obvious impact.

According to HUD in FY 2010, "Nearly 58 percent of borrowers (of FHA loans) had credit scores of 680 or better, while only four percent had credit scores below 620. As recently as the last half of 2008, less than 20 percent of borrowers had credit scores of 680 or better and 45 percent had credit scores below 620."[18] A significant factor behind this dramatic shift in credit score distribution is lender policies of refusing to lend to borrowers with credit scores below 640.

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[17] See the Woodstock Institute, Bridging the Gap: Credit Scores and Economic Opportunity in Illinois Communities of Color, September 2010, via www.woodstockinst.org. Woodstock used data as of June 2009 from a large national credit bureau.

[18] Department of Housing and Urban Development, *FHA Single Family Mutual Mortgage insurance Fund Programs, Quarterly Report to Congress,* FY 2010, Q4, November 4, 2010.

Conclusion

NCRC's investigation reveals that the majority of the country's largest FHA lenders are refusing to lend under the FHA loan program to consumers with credit scores between 580 and 640, despite the fact that FHA policy is for approved-lenders to extend credit to consumers with credit scores at 580 and above. Nearly one-third of all Americans have credit scores below 620, thus, an enormous qualified segment of the American public is being denied the possibility of homeownership. To make matters worse, NCRC has discovered that many lenders are moving to increase their minimum credit score requirements. This would deny credit opportunities to millions of potential homeowners. Serving only the "credit elite" is an arbitrary decision in this instance, and has no legitimate business justification.

This widespread policy has shocking consequences for consumers, their families, and our economy. Not only do these policies deny access to qualified homeowners seeking to avoid foreclosure by obtaining an FHA loan, it also limits the ability of homeowners seeking to purchase a home, including on vacant properties. This will prevent many properties from contributing to local tax bases. This arbitrary suppression of the impact that the FHA program could have, works against stabilizing home values and economic recovery as a whole. Ultimately, these policies are in direct opposition to the purpose and intent of the FHA loan program, which was created during the Great Depression to help Americans secure access to credit in order to realize or sustain homeownership at a time when the private lending market was nearly frozen.

In addition to stunting our economic recovery, this policy has a disproportionate and adverse impact on African-American and Latino individuals, families, and communities. Recent Home Mortgage Disclosure Act data, Lender Processing Services data, and regulatory reports clearly demonstrate the significant role FHA has played in originating loans to minority consumers. By denying access to FHA loans for qualified, creditworthy individuals, without justification for the actual risk posed by the loan to the financial institution, lenders are discouraging the flow of credit and capital into communities of color and modest income neighborhoods. These policies amount to discrimination in violation of the federal Fair Housing Act, the Equal Credit Opportunity Act, and the Community Reinvestment Act.

As such, NCRC has called on U.S. Departments of Justice and Housing and Urban Development, the Federal Reserve, the Federal Deposit Insurance Corporation, the Office of Thrift Supervision, and the Office of the Comptroller of the Currency and the Consumer Financial Protection Bureau to investigate and end these practices. In addition, NCRC calls on our nation's lenders to voluntarily revise their policies and to extend credit, in a safe and sound manner, to all hardworking Americans based on their ability to pay and other strong underwriting standards. Doing so will not only help strengthen our economic recovery, but will ensure that all Americans, regardless of race, are able to access credit and the window to prosperity it can provide.

Appendix A

As of December 6, 2010, NCRC has begun an investigation of the top 50 FHA lenders and is filing to HUD regarding 22 lenders. Investigations are ongoing. The 22 lenders that NCRC has filed against so far - and their minimum credit score restrictions - are:

1. **AMERICAN EQUITY MORTGAGE, INC. 640**
2. **AMERICAN FINANCIAL RESOURCES**
3. **BANK OF THE WEST 620**
4. **BANCO BILBAO VIZCAYA 620**
5. **CITIZENS FINANCIAL 620**
6. **ENVOY MORTGAGE 640**
7. **FIRST RESIDENTIAL MORTGAGE 620**
8. **FRANKLIN AMERICAN MORTGAGE CO 620**
9. **FREEDOM MORTGAGE CORP. 620**
10. **METLIFE BANK, N.A. 620**
11. **NATIONSTAR MORTGAGE LLC 620**
12. **NEW DAY FINANCIAL, LLC 620**
13. **NEW PENN FINANCIAL, LLC 620**
14. **PARAMOUNT RESIDENTIAL MORTGAGE 640**
15. **PHH MORTGAGE CORPORATION 620**
16. **PROSPECT MORTGAGE, LLC 640**
17. **SECURITYNATIONAL MORTGAGE 620**
18. **SHORE MORTGAGE 640**
19. **SIERRA PACIFIC MORTGAGE CO. 620**
20. **STEARNS LENDING, INC. 640**
21. **SYNOVUS/ BANK OF NORTH GEORGIA 620**
22. **WR STARKEY MORTGAGE, LLP 640**

Appendix B
Mystery Shopping Vignettes

In our investigation of FHA-approved lenders, NCRC uncovered several instances of immediate and arbitrary loan denials. Below are a few vignettes of how our testers were treated when they sought credit from these institutions.

> *An NCRC tester called an FHA Lender, seeking a mortgage to purchase a home with his wife, with credit scores of 601 and 605. The lender's representative stated that there were no loans available with those credit scores, because the lender required a minimum credit score of 620. Instead, the lender suggested that our testers turn to a credit union for their needs.*
>
> *An NCRC's tester called an FHA Lender, seeking a mortgage to purchase a home with his wife, with credit scores of 610 and 615. The lender's representative stated that the tester was unable to get any loans, because of their corporate policy establishing a minimum credit score of 640 which has been in place for the last six months. When the tester said that he had seen information on FHA loan, the representative stated that she was not aware of any programs like that.*
>
> *NCRC's tester contacted a Philadelphia branch of a large FHA lender. The tester indicated that she and her husband had credit scores of 601 and 605 and wanted to see what kind of a loan they would be able to get. The lender's representative sighed and then said "none" because the minimum credit score for an FHA loan was 620 and that it was actually going to be going up to 640 next month. Despite having more than enough of a down payment, the representative indicated that he wouldn't be able to help them.*

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