

April 3, 2006

## FREQUENTLY ASKED QUESTIONS ABOUT THE NEW HMDA DATA

### General Background

#### 1. What is the Home Mortgage Disclosure Act (HMDA)?

HMDA, enacted by Congress in 1975, requires most mortgage lenders located in metropolitan areas to collect data about their housing-related lending activity, report the data annually to the government, and make the data publicly available. Initially, HMDA required reporting of the geographic location of originated and purchased home loans. In 1989, Congress expanded HMDA data to include information about denied home loan applications, and the race, sex, and income of the applicant or borrower. In 2002, the Federal Reserve Board (the Board) amended the regulation that implements HMDA (Regulation C) to add new data fields, including price data for some loans (see Q. 9). HMDA does not prohibit any lending activity, nor is it intended to encourage unsound lending practices or the allocation of credit.

#### 2. What are the purposes of HMDA?

Congress enacted HMDA to:

- provide the public with information to judge whether lenders are serving their communities;
- enhance enforcement of laws prohibiting discrimination in lending; and
- provide private investors and public agencies with information to guide investments in housing.

#### 3. What are HMDA data?

HMDA data cover home purchase and home improvement loans and refinancings, and contain information about loan originations, loan purchases, and denied, incomplete or withdrawn applications. With some exceptions, for each transaction the lender reports data about:

- the loan (or application), such as the type and amount of the loan made (or applied for) and, in limited circumstances, its price;
- the disposition of the application, such as whether it was denied or resulted in an origination of a loan;
- the property to which the loan relates, such as its type (single-family vs. multi-family) and location (including the census tract);
- the applicant's ethnicity, race, sex, and income; and
- the sale of the loan, if it was sold.

In 2004, HMDA data included a total of 33 million reported loans and applications. More information about HMDA data can be found at <http://www.ffiec.gov/hmda>.

#### **4. Are all home mortgage loans covered by HMDA?**

Most home-secured loans are included in HMDA data. Some, however, are not included. For example, a home equity loan taken out for consolidation of credit-card debt or to pay for medical expenses is not covered by HMDA, unless some part of the loan proceeds are also intended for home improvement or home purchase purposes. Home equity lines of credit (HELOCs) may not be in the data even if intended for home improvement or home purchase because reporting HELOCs is optional. Additionally, not all mortgage lenders are HMDA reporters. For example, a lender does not have to report HMDA data unless it has an office in a metropolitan statistical area (MSA). As a result, reporting of home loans made in some rural areas may be relatively low.

#### **5. When, and in what forms, are HMDA data made available to the public?**

March 31 is the earliest date that data from the previous calendar year are required to be publicly available. That is the date by which an institution must respond to any request it receives by March 1 for its “loan application register” (LAR). The LAR is the format for data disclosure required by law. It itemizes reportable transactions application by application, loan by loan. Lenders are not required, however, to arrange transactions on the LAR in any particular order (for example, by branch or by type of loan). Any member of the public may request a modified LAR from any lender covered by HMDA. To help preserve consumer privacy, the law requires lenders to remove the loan or application number and the application and action-taken dates before making the LAR public.

September 2006 is the expected publication date for summary tables of the 2005 data. The tables are published by the Federal Financial Institutions Examination Council (FFIEC). Summary tables will be available on three levels. A summary is published for every mortgage lender, broken down by each metropolitan area in which it does business; for every metropolitan area, aggregating information about different lenders’ activity in the area; and for the nation as a whole. For more information about the tables and how to get them, go to <http://www.ffiec.gov/hmda>.

#### **6. How do government agencies use HMDA data?**

Government agencies use HMDA data to assist in evaluating lender compliance with anti-discrimination laws and other consumer protection laws. The anti-discrimination laws include the Equal Credit Opportunity Act (ECOA) and the Fair Housing Act (FHA). These laws prohibit discrimination in home mortgage lending, among other things, on several bases such as race, national origin, sex, and, in the case of ECOA, age. For more information on ECOA and FHA, see the *Policy Statement on Discrimination in Lending*, 59 Fed. Reg. 18266 (April 15, 1994), available at <http://www.fdic.gov/regulations/laws/rules/5000-3860.html>.

Government agencies use HMDA data to identify institutions, loan products, or geographic markets that show disparities in loan applications or originations by race, ethnicity, or other characteristics that may warrant further investigation under ECOA or FHA. With the addition of price data for higher-priced loans, the agencies are also able to identify in the HMDA data price disparities that may warrant further investigation (see Q. 13, 15 and 16). If disparities are found to violate ECOA or FHA, certain federal agencies are authorized to compel lenders to cease discriminatory practices and, among other remedies, obtain monetary relief for victims.

In addition, the agencies responsible for evaluating insured depository institutions under the Community Reinvestment Act (CRA) use HMDA data to evaluate institutions' records of helping to meet community mortgage credit needs. For more information about CRA, go to <http://www.ffiec.gov/cra>.

## **7. Who reports HMDA data?**

Banks, savings and loan associations, credit unions, and mortgage and consumer finance companies are required to report HMDA data if they meet the law's criteria for coverage. Generally, whether a lender is covered by HMDA depends on:

- The lender's asset size (for example, an institution with assets of \$34 million or less on December 31, 2004, did not have to collect HMDA data in 2005);
- Whether the lender has an office in a metropolitan statistical area; and
- The extent of the lender's housing-related lending activity.

In 2005, 8,853 lenders reported 2004 HMDA data. For more information about the law's criteria for coverage, go to <http://www.ffiec.gov/hmda/pdf/2004guide.pdf>.

## **8. What is the Federal Reserve Board's role in HMDA?**

Congress authorized the Federal Reserve Board (the Board) to write rules to carry out HMDA. The Board's HMDA rules are known as Regulation "C" (12 CFR Part 203). The Board also provides guidance about HMDA through a staff commentary (12 CFR Part 203, Supp. I). Additionally, the Board assists the FFIEC in publishing the manual, "A Guide to HMDA Reporting: Getting it Right!" (available at <http://www.ffiec.gov/hmda/pdf/2004guide.pdf>), processing the reported data, and publishing summary tables each year (see Q. 5).

### **Price Data on "Higher-Priced Loans"**

## **9. What price data are available under HMDA?**

The price data take the form of a "rate spread." Lenders must report the spread (difference) between the annual percentage rate (APR) on a loan and the rate on Treasury securities of comparable maturity – but only for loans with spreads above designated thresholds. So rate spreads are reported for some, but not all, reported home loans.

The APR represents the cost of credit to the consumer. It captures not just the contract-based interest rate on a loan, but also the points and fees that a consumer pays and other finance charges such as premiums for private mortgage insurance. Lenders must calculate and disclose the APR to consumers under a separate law, the Truth in Lending Act.

Lenders also report price information in the form of a “flag” indicating whether a loan exceeds the price triggers of the Home Ownership and Equity Protection Act (HOEPA). Those triggers are substantially higher than the thresholds for reporting rate spreads. The rate-spread thresholds and the HOEPA triggers are discussed below (see Q. 10, 20).

**10. Which loans are deemed “higher-priced” and therefore have their prices reported?**

A loan’s rate spread (see Q. 9) must be reported if the spread exceeds the threshold set by the Board in Regulation C. For first-lien loans, the threshold is three percentage points above the Treasury security of comparable maturity; for second-lien loans, which tend to have higher prices, the threshold is five percentage points above the Treasury security of comparable maturity. The Board chose the thresholds in the belief that they would exclude the vast majority of prime-rate loans and include the vast majority of subprime-rate loans. From year to year, however, the proportion of subprime-rate loans that have their prices reported may vary because of changes in the interest rate environment (see Q. 27).

**11. Why is the requirement to report price data limited to higher-priced loans?**

The higher-priced mortgage market has grown substantially in the last decade. Its expansion has afforded some consumers greater access to home mortgage credit. The growth of the higher-priced mortgage market, however, has raised concerns that consumers in this market lack the information needed to negotiate the best terms and may be vulnerable to unfair or deceptive practices. Also, the wider range of prices in this market has raised concerns that price differences may reflect unlawful discrimination rather than legitimate risk- and cost-related factors.

In contrast, the prime market’s limited variation in prices helps allay concerns about market efficiency and consumer protection. Though the prime market is not without risk of unlawful discrimination or violation of other consumer protection laws, the banking agencies use their routine examinations of depository institutions to address that risk (see Q. 16).

**12. Is price information reported on all mortgage loans that have prices above the price reporting thresholds?**

Price information is reported on most, but not all, loans that have prices above the price reporting thresholds. Under Regulation C, some loans are not reportable at all, such as home equity loans for consolidation of debt (see Q. 4). Moreover, for certain kinds of

loans that Regulation C requires be reported, a lender need not report price information. Examples in this category include unsecured home improvement loans, assumptions, and loans purchased from other lenders (though purchased loans would likely have been reported by the original lenders). Finally, reporting information about home equity lines of credit (HELOCs) is optional; a lender opting to report HELOCs need not report price information.

**13. To the extent the HMDA data indicate that minorities pay more for loans than whites on average, does that difference prove unlawful discrimination?**

No. However, such a disparity may indicate a need for closer scrutiny. Supervisory and enforcement agencies investigating disparities typically collect additional information about factors that may determine loan prices from lenders' loan files or other sources. Without information about relevant price determinants, one cannot draw definitive conclusions about whether particular lenders discriminate unlawfully or take unfair advantage of consumers. HMDA data include some potentially relevant determinants of price, such as lien status, but exclude many other potential determinants, such as borrower credit history, borrower debt-to-income ratio, and the ratio of the loan amount to the value of the property securing the loan (loan-to-value ratio). Therefore, price disparities by race, ethnicity, or sex disclosed in HMDA data will not alone prove unlawful discrimination.

**14. Why aren't all pricing factors reported in HMDA data?**

In 2002, when the Board adopted the requirement to report price data and lien status, an important determinant of loan price, the Board considered adding to HMDA data other data items relevant to loan pricing, such as loan-to-value ratio. For each possible new data item, the Board weighed the potential benefit and burden that would result, such as the costs of collection and reporting. On the basis of that analysis, which relied in part on public comments, the Board decided not to add more factors.

**15. If HMDA data cannot support definitive conclusions about whether price differences reflect unlawful discrimination, then what is the point of requiring disclosure of price data?**

Though the price data do not support definitive conclusions, they are a useful screen, previously unavailable, to identify lenders, products, applicants, and geographic markets where price differences among racial or other groups are sufficiently large to warrant further investigation. Enforcement and supervisory agencies can use the HMDA price data to better target their resources. HMDA price data can also be a valuable part of any mortgage lender's self-evaluation program.

**16. What other tools beside the HMDA price data are used to detect price discrimination?**

The federal banking agencies analyze HMDA price data in conjunction with other information to evaluate the potential for price discrimination. The Interagency Fair Lending Examination Procedures direct examiners to identify risk factors for discrimination by reviewing a variety of information, including an institution's records, to understand the institution's fair lending compliance management program. Examiners evaluate a lender's risk of price discrimination based on several factors, including the relationship between loan pricing and compensation of loan officers or brokers; the presence of broad pricing discretion; the use of a system of risk-based pricing that is not empirically based and statistically sound; substantial disparities among prices quoted or charged to applicants who differ in their protected characteristics such as race or ethnicity; and consumer complaints alleging price discrimination. The HMDA price data are analyzed in conjunction with these other factors to determine the level of risk of price discrimination. The level of risk of price discrimination, in turn, is one of the factors examiners consider when determining the depth and breadth of a fair lending examination by a federal banking agency.

## **17. Why do some borrowers pay higher prices than others?**

Many factors affect the price of a mortgage loan. Some factors, such as a borrower's credit history, debt-to-income (DTI) ratio, or the ratio of the loan amount to the value of the property that secures the loan (LTV), are used by lenders to set loan prices because they have been shown to predict whether or not borrowers will pay their loans as agreed. Generally, borrowers with poor credit histories or high DTI or LTV ratios represent increased risk of non-payment, which lenders offset with a higher price to such borrowers.

Other factors that may affect loan price include the price the lender pays for the money it lends to borrowers ("cost of funds"), the type of loan product and whether its rate and terms are fixed or variable, whether the lender holds its loans in portfolio or sells them in the secondary market, and whether the lender extends credit through its own loan officers or independent brokers. Discretionary pricing by loan officers and brokers can also produce differing loan prices, although discretionary pricing is not, by itself, unlawful. Unfortunately, price disparities may also be the result of unfair or deceptive behavior by lenders or brokers, or unlawful discrimination on the basis of race, ethnicity, or sex.

## **18. How can a consumer obtain the best price on a loan?**

It is important that borrowers shop, compare, and negotiate the price and other terms of their loans. For more information about shopping for a mortgage loan, go to [www.mymoney.gov](http://www.mymoney.gov) or call 1-888-MYMONEY.

### **Data on HOEPA Loans**

## **19. Lenders are required to report a loan's HOEPA status. What is HOEPA?**

Lenders are required to report whether a loan is subject to the provisions of the Home Ownership and Equity Protection Act (HOEPA). HOEPA, enacted as part of the Truth in Lending Act, imposes substantive limitations and additional disclosures on certain types of home mortgage loans with rates or fees above a certain percentage or amount. For more information about HOEPA, see the Board's Regulation Z, 12 CFR part 226, sections 31, 32 and 34.

**20. What is the difference between a HOEPA loan and a higher-priced loan reported under HMDA?**

Many, but not all, HOEPA loans are reported under HMDA; there are some kinds of home equity loans that HOEPA covers that HMDA does not require to be reported (see Q. 4). Moreover, only a minority of loans that have their rate spreads reported under HMDA are HOEPA loans, because HMDA's threshold rate for reporting a loan's rate spread is much lower than the threshold rate for HOEPA's coverage of a loan. On first lien loans, for example, HMDA-reportable loans must have their rate spread reported if the APR exceeds the yield on comparable Treasury securities by three or more percentage points (see Q. 9, 10), while HOEPA covers loans with APRs that exceed the comparable Treasury yield by more than eight percentage points – a much higher threshold. An alternative test for HOEPA coverage (whether the points and fees exceed 8 percent of the total loan amount) also sets a high threshold. In short, Congress limited HOEPA's protections and disclosures to the highest-priced loans in the subprime home mortgage market, while the Board set HMDA's price thresholds to include the vast majority of subprime-rate mortgage loans.

**21. Does the requirement in Regulation C to report HOEPA status impose any new obligations on lenders?**

Under the amendments to Regulation C, lenders are required to report whether a loan is subject to the requirements of HOEPA. The amendments to Regulation C do not, however, affect any of HOEPA's requirements or limitations. Lenders should already have in place procedures for monitoring and complying with the provisions of HOEPA.

**Other Items in HMDA Data that Aid Interpretation of Price Data**

**22. Why must lenders report the lien status of a loan?**

Lenders report whether a loan is or would be secured by a lien on a dwelling and, if so, whether a first lien or a subordinate (junior) lien. A loan's lien status determines what rate-spread reporting threshold applies to the loan (see Q. 9, 10). Also, because lien status is an important determinant of loan price (interest rates on first-lien loans are generally lower than rates on junior-lien loans), lien status differences may explain some price disparities.

**23. Why must lenders identify loans involving manufactured homes?**

HMDA has long required lenders to identify whether a loan or application involved a one-to-four family home or a multi-family home. Lenders also must identify whether a loan or application involves a manufactured home. Generally speaking, manufactured homes are factory-built homes essentially ready for occupancy when they leave the factory. The market for credit to finance manufactured home purchases is somewhat different from the market for credit to finance site-built home purchases. For example, applications for manufactured home financing are denied at much higher rates than applications for site-built home financing. Identification of manufactured home loans will make it easier to identify the sources of differences in denial rates, and will improve understanding of manufactured home financing.

### **Year-To-Year Comparison of HMDA Data**

#### **24. How has the reporting of borrower ethnicity and race under HMDA changed?**

In 2002, the Board amended Regulation C's rules for collection of information about applicants' ethnicity and race, to conform them to revised standards of the Office of Management and Budget (OMB) for collection of such data. These standards are available at <http://www.whitehouse.gov/omb/fedreg/1997standards.html>. The new rules for collecting ethnicity and race information under HMDA became effective with the collection of 2004 data. Therefore, the change may complicate comparisons based on race between HMDA data preceding 2004 and HMDA data from 2004 and later years. For more information about the changes, go to <http://www.federalreserve.gov/boarddocs/press/bcreg/2004/20041210/attachment2.pdf>

#### **25. How will changes in OMB's standards for defining metropolitan and micropolitan statistical areas affect comparison of HMDA data preceding 2004 with data from 2004 and later years?**

HMDA requires the use of metropolitan statistical areas defined by OMB for a variety of purposes: determining whether a lender has reporting obligations, reporting property location, providing disclosures and reports of lending activity, and posting notices about the availability of HMDA data. For HMDA data collected in 2003 and previous years, OMB's 1990 standards for defining MSAs were in effect. OMB's 2000 standards, however, apply to HMDA data collected in 2004 and later years. The application of the new OMB standards will, therefore, affect comparisons of HMDA data for 2004 and later years with data for previous years. For more information, go to <http://www.federalreserve.gov/boarddocs/press/bcreg/2003/20031219/attachment.pdf>

#### **26. How do the transition rules affect the HMDA data?**

HMDA requires lenders to report data about an application in the year in which the application was denied or resulted in an origination. The 2002 amendments to HMDA took effect on January 1, 2004. The Board provided guidance, in the form of transition rules, to assist lenders in collecting and reporting data for applications received before

January 1, 2004, but not acted on until later. For more information, go to <http://www.ffiec.gov/hmda/pdf/transitionrules.pdf>

The transition rules primarily affect lenders' 2004 data but could also affect their 2005 data in unusual cases in which applications taken before 2004 were not acted on until 2005. To help data users isolate the effects of the transition rules, the FFIEC flagged applications taken before 2004 in the lender disclosure reports and aggregate reports for 2004 data released in September 2005; the FFIEC will also flag pre-2004 applications in the reports for 2005 data to be released in September 2006. In addition, lenders were encouraged to flag applications taken before 2004 on their 2004 Loan Application Registers.

**27. How should year-to-year changes in the number or proportion of loans with prices above the HMDA price reporting thresholds (higher-priced loans) be interpreted?**

Year-to-year changes in the number or proportion of loans with prices that exceed the thresholds for reporting price information (higher-priced loans) should be interpreted with great care. Changes in the number or proportion of higher-priced loans could be due to changes in the interest rate environment – specifically, in the relationship between short-term and long-term interest rates. Such changes also could be due to changes in lenders' business practices or consumers' borrowing practices or risk profiles.

The "yield curve" displays how the yield on an instrument varies with its maturity and, therefore, it reflects the relationship between short-term and long-term interest rates. The yield curve is typically upward-sloped, that is, short-term rates are typically lower than long-term rates. Sometimes, however, the yield curve is flat, that is, short-term rates are sometimes close to long-term rates. And, occasionally, the yield curve inverts, so that short-term rates are above long-term rates.

Changes in the shape of the yield curve, that is, the relationship between short-term and long-term interest rates, can affect the reporting of higher-priced loans. Lenders usually use relatively short-term interest rates to set mortgage rates (for example, interest rates on maturities of less than ten years); but, for most loans, Regulation C requires lenders to use long-term rates (20 years or more) to determine whether to report a loan as higher-priced. Thus, a change from one year to the next in the relationship between short-term rates and long-term rates will cause a change from one year to the next in the proportion of loans that are reported as higher-priced loans, all other things being equal. For example, if short-term rates rise more than long-term rates, then the number and proportion of loans reported as higher-priced loans will increase if all other factors that may influence the number and proportion of higher-priced loans, such as the business practices of lenders and the risk profiles and borrowing practices of borrowers, remain constant. Conversely, if short-term rates fall more than long-term rates, then the number and proportion of loans reported as higher-priced loans will fall if all other potentially influential factors remain constant. It is also possible that the number or proportion of

loans reported as higher-priced could change in response to both a change in the interest rate environment and to changes in other factors.

Short-term interest rates rose over 2004 and 2005, while long-term rates fell over 2004 and were relatively stable over 2005. Thus, while in 2004, short-term rates were well below long-term rates, by the end of 2005, short-term rates and long-term rates were fairly close. Accordingly, one would expect a higher proportion of loans originated in 2005 than of loans originated in 2004 to be reported under HMDA as higher-priced loans. Changes in other factors, such as the business practices of lenders or the risk profiles or borrowing practices of borrowers, also could have affected the proportion of loans reported as higher-priced loans.