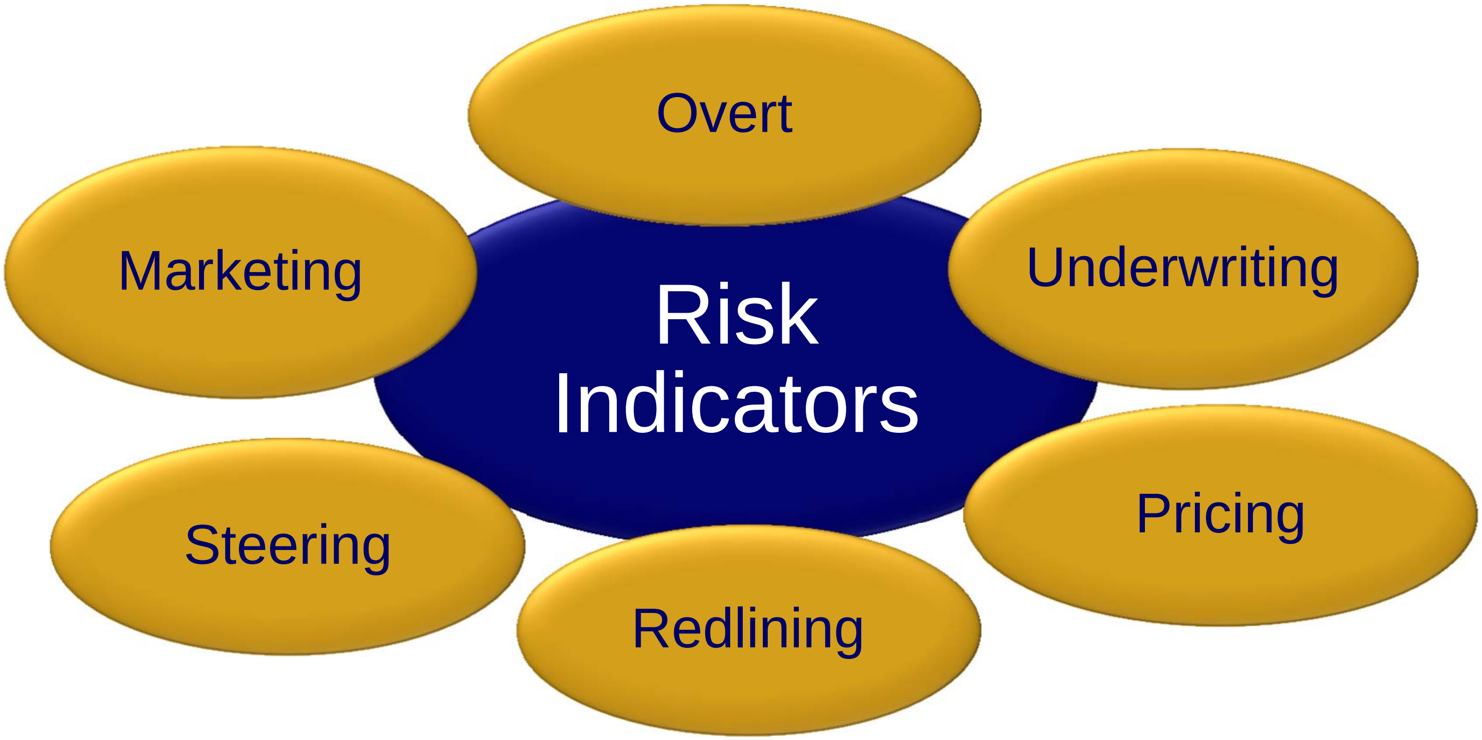
FEDERAL DEPOSIT INSURANCE CORPORATION

Managing Fair Lending Risk

III. Fair Lending Risk Indicators – Part II

Fair Lending Risk Indicators



Redlining

Redlining is a form of illegal discrimination in which a bank provides unequal access to credit, or unequal terms of credit on a prohibited basis based on the location of the applicant's residence.

Redlining

Redlining does not necessarily mean the total absence of lending within minority areas. It can also be identified when a bank's lending level in minority areas is not comparable with lending levels in non-minority areas, especially when factors such as competition, demographics, and economic conditions are considered.

Redlining Risk Indicators

- Lack of applications from or lending in minority areas;
- Disproportionately high denial rates for applicants located in minority areas;
- Arbitrary exclusion of minority areas from the bank's market area or CRA Assessment Area;
- Differences in services or hours of operation at branches in minority versus non-minority areas; and
- Lack of branches in minority areas.

Strategies

Define the bank's market areas based on legitimate business reasons.

Monitor loan activity by the racial composition of census tracts to detect possible discriminatory trends.

Ensure marketing efforts encompass the entire market area.

Ensure differences in products, hours, and services between branches are due to legitimate business reasons.

Key Fact to Remember

The bank should know the demographics of its market area and the lending activity in and around that area.

Steering

Steering is the practice of deliberately guiding loan applicants toward or away from certain loan products or lending channels on a prohibited basis.

Steering Risk Indicators

A lack of clear, objective, and consistently implemented standards for:

- Referring applicants to subsidiaries, affiliates, or lending channels within the bank;
- Classifying applicants as “prime” or “sub-prime” borrowers; or
- Deciding what kinds of alternative loan products should be offered or recommended to applicants.

Steering Risk Indicators

- Financial incentives to place applicants in nontraditional or higher-cost products;
- Significant differences in percentages of prohibited basis groups in each of the alternative loan products; or
- Significant differences in the percentages of prohibited basis applicants in one of the lending channels when compared to that of another lending channel.

Steering - Example

Borrower	In-House Mortgage Loans	Secondary Market Mortgage Loans
Hispanic	685 / 85%	125 / 15%
Non-Hispanic White	225 / 10%	1,985 / 90%

Strategies

Establish standards for referring applicants to subsidiaries, affiliates, or other lending channels.

Ensure loan officers inform applicants about available products and consumers decide which option is best.

Review and monitor loan distribution by lending channel or product for differences on a prohibited basis.

Review loan officer compensation agreements.

Key Fact to Remember

Banks should have a process in place to ensure that applicants select the loan channels and products that best suit their needs and qualifications.

Marketing Risk Indicators

- Advertising methods that discourage individuals on a prohibited basis from applying for loans;
- Advertising only in media that serve non-minority areas within the bank's market area; and
- Significantly lower levels of applications from prohibited basis groups than their representation in the total population of the bank's market area.

Marketing - Example

Borrower	% of Population	Application Rate
Asians	20	2%

Strategies

Ensure marketing efforts do not exclude specific regions or geographies within the bank's market or CRA assessment areas.

Review loan application distributions to determine whether patterns exist that raise marketing concerns.

HMDA Reporters should review distribution of applications by race, gender, ethnicity, or location. Compare application rates for each group to the demographics of the lending area.

Key Fact to Remember

Marketing efforts should encompass all segments of a bank's market area.

SUMMARY

Fair Lending Risk Indicators – Part II

- Redlining
- Steering
- Marketing

SUMMARY

- **Redlining:** Not necessarily a total absence of lending in minority areas, but a lack of lending when compared to factors such as demographics, competition, and economic conditions.
- **Steering:** Guiding potential applicants to a lending channel or product should be based on nondiscriminatory criteria. Ultimately, the applicants should select the loan channels and products that best suit their needs and qualifications.
- **Marketing:** Should encompass the bank's entire market area.

SUMMARY

Complaints can also provide valuable insight and direct management's attention toward areas that present fair lending risk.