United States Government Accountability Office

Report to Congressional Requesters

February 2018

COMMUNITY REINVESTMENT ACT

Options for Treasury to Consider to Encourage Services and Small-Dollar Loans When Reviewing Framework

GAO-18-244

GAO
Highlights

Highlights of GAO-18-244, a report to congressional requesters

Why GAO Did This Study

A 2015 FDIC survey found that 7 percent of U.S. households were unbanked—meaning no one had a checking or savings account—and about 20 percent were underbanked—meaning the household had such an account but used an AFS provider's products. The goal of CRA is to encourage financial institutions to help meet the credit needs of the communities in which they operate, including LMI neighborhoods. FRB, FDIC, and OCC periodically evaluate financial institutions' efforts to meet the credit needs of their communities.

GAO was asked to assess financial institutions' provision of basic banking services and small-dollar, nonmortgage consumer loans in LMI communities, including how regulators evaluate their performance. GAO assessed 2016 data on the availability of financial institutions in LMI communities; reviewed regulators' evaluation procedures; and analyzed a generalizable, stratified random sample of 219 CRA performance evaluations from 2015 to determine how provision of these services and loans was assessed. GAO also solicited input from stakeholders (including consumer advocacy groups, financial industry members, and regulators) through methods including interviews, a survey, and panel discussions.

What GAO Recommends

GAO recommends that Treasury consider the options outlined in this report when conducting its planned review of the CRA framework. Treasury concurred with the recommendation.

View GAO-18-244. For more information, contact Alicia Puente Cackley at (202) 512-8678 or cackleya@gao.gov.

February 2018

COMMUNITY REINVESTMENT ACT

Options for Treasury to Consider to Encourage Services and Small-Dollar Loans When Reviewing Framework

What GAO Found

Based on GAO analysis of 2014 and 2016 data from the Federal Deposit Insurance Corporation (FDIC), National Credit Union Administration, Federal Financial Institutions Examination Council, and Census, low- and moderate-income (LMI) communities have at least as many banks and credit unions nearby as middle-income communities in rural areas and larger metropolitan areas but fewer than in smaller metropolitan areas. However, 2015 FDIC survey data suggest lower-income households were more likely to obtain credit or conduct financial transactions through an alternative financial services (AFS) provider (such as a check casher) and less likely to have a checking or savings account with a bank or credit union than their higher-income counterparts.

Federal banking regulators' procedures for conducting Community Reinvestment Act (CRA) evaluations do not require an evaluation of financial institutions' provision of retail banking services or small-dollar, nonmortgage consumer lending, or support for community development in LMI areas for every institution. Whether the federal banking regulators—the Board of Governors of the Federal Reserve System (FRB), FDIC, and Office of the Comptroller of the Currency (OCC)—evaluate a financial institution on its provision of these services and loans depends on the type of institution, among other factors. For example, while large institutions are subject to evaluations of their services, lending, and support of community development, smaller institutions are primarily evaluated on their lending. Further, small-dollar, nonmortgage consumer lending is typically evaluated only if consumer lending is a substantial majority of the lending or a major product of the institution, which generally is not the case across all institution types.

Stakeholders GAO contacted identified several options they believe could provide additional incentives for financial institutions to provide basic banking services and small-dollar, nonmortgage consumer loans in LMI areas. Such options include modifications to tests conducted as part of the CRA examination process to focus more on the extent to which institutions are offering these services and loans, expanding the areas and entities assessed as part of the examinations, and clarifying guidance about the examination process. However, other stakeholders noted that such options may not alleviate institutions' competing concerns about the profitability of these services and loans or regulators' concerns about their safety and soundness. In commenting on these options, the federal banking regulators noted they had, among other things, issued in 2016 additional guidance on small-dollar loans that would qualify for CRA consideration. In June 2017, the Department of the Treasury issued a report indicating that statutes of critical importance to the banking sector, such as CRA, should be modernized to better target the financial risks consumers face. As a result, Treasury is planning a review of how CRA is being implemented, though the agency did not have a timeline for completing this review. Given the continuing unmet needs of many LMI consumers in obtaining basic banking services and small-dollar credit, the options that our work identified could help inform Treasury's review of the CRA framework and potentially encourage financial institutions to provide basic banking services and small-dollar, nonmortgage loans.

Contents

Letter		1
	Background	4
	Financial Services Providers' Availability to Lower-Income Consumers Varies by Location, and Lower-Income Consumers Are More Likely to Use Alternative Providers	10
	While Limited for Certain Institutions, Scope of CRA Evaluations Was Consistent with Examination Procedures	21
	Suggested Options Reflect Need to Balance Serving LMI Consumers with Concerns about Profitability and Safety and Soundness	34
	Conclusions	52
	Recommendation for Executive Action	52
	Agency Comments	53
Appendix I	Objectives, Scope, and Methodology	54
Appendix II	Analysis of Availability of Financial Products and Services to Low- and Moderate-Income Communities	59
Appendix III	Econometric Analysis of Household Income and Use of Financial Products and Services	75
Appendix IV	Additional Information on Options That Could Further Encourage Banking Services and Small-Dollar Loans	93
Appendix V	Comments from the Department of the Treasury	110
Appendix VI	GAO Contact and Staff Acknowledgments	111

Tables

Table 1: Estimated Differences in Number of Bank and Credit Union Branches Nearby Low- and Moderate-Income Communities Relative to Middle-Income Communities, by Location Type, 2016 12
Table 2: Estimated Differences in Use of Banks and Credit Unions by Lower-Income Households Relative to Households with Annual Income of $75,000 or More, 2015 17
Table 3: Estimated Differences in Use of Alternative Financial Services Providers by Lower-Income Households Relative to Households with Annual Income of $75,000 or More, 2015 19
Table 4: Estimated Differences in Saving, Bill-Paying, and Consumer Credit Behaviors for Lower-Income Households Relative to Households with Annual Income of $75,000 or More, 2015 20
Table 5: Population and Sample of 2015 Community Reinvestment Act Performance Evaluations, by Examination Type 56
Table 6: Census Tract Income Group Definitions 59
Table 7: Numbers of Census Tracts and Percentage of Population in Census Tracts, by Income and Location Type, 2016 60
Table 8: Characteristics of Census Tracts, by Income and Location Type, 2016 61
Table 9: Numbers of Bank and Credit Union Branches Nearby Census Tracts with Different Income Levels, by Location Type, 2016 64
Table 10: Number of Census Tracts with No Bank and Credit Union Branches Nearby, by Income Level and Location Type, 2016 65
Table 11: Number of Large Bank Community Reinvestment Act Assessment Areas Containing Census Tracts, by Income and Location Type, 2015 66
Table 12: Number of Alternative Financial Services Establishments per 10,000 People in Counties, by Location Type, 2014 66
Table 13: Ratio of Bank and Credit Union Branches Nearby Low, Moderate-, and Upper-Income Census Tracts to Branches Nearby Similar Middle-Income Tracts, by Location Type, 2016 69

Table 14: Ratio of Bank and Credit Union Branches Nearby Low-, Moderate-, and Upper-Income Census Tracts to Branches Nearby Similar Middle-Income Tracts, by Metropolitan Area, 2016 70
Table 15: Ratio of Number of Large Bank Community Reinvestment Act Assessment Areas Containing Low-, Moderate-, and Upper-Income Census Tracts to Number Containing Similar Middle-Income Tracts, 2015 73
Table 16: Changes in Alternative Financial Services Establishments in Counties Associated with Changes in Population in Low-, Moderate-, and Upper-Income Census Tracts, 2014 74
Table 17: Household Responses to Questions Related to Basic Banking Services, 2015 76
Table 18: Household Responses to Questions Related to Small-Dollar, Unsecured Loans, 2015 78
Table 19: Characteristics of Households and Heads of Households, 2015 80
Table 20: Estimated Differences in Methods for Obtaining Basic Banking Services for Lower-Income Households Relative to Households with Annual Income of $75,000 or More, 2015 84
Table 21: Estimated Differences in Methods for Accessing Checking and Savings Accounts for Lower-Income Households Relative to Households with Annual Income of $75,000 or More, 2015 86
Table 22: Estimated Differences in Reasons for Not Having Checking or Savings Accounts for Lower-Income Households Relative to Households with Annual Income of $75,000 or More, 2015 87
Table 23: Estimated Differences in Savings, Bill Paying, and Consumer Credit Behaviors for Lower-Income Households Relative to Households with Annual Income of $75,000 or More, 2015 89

Figures

Figure 1: Number of Bank Branches, Credit Union Branches, and Alternative Financial Services (AFS) Establishments Nationwide, 2005 through 2016 10
Figure 2: Numbers of Bank and Credit Union Branches per 10,000 People by County, 2016 (number of counties) 13

Figure 3: Number of Alternative Financial Services Establishments per 10,000 People by County, 2016 (number of counties) 15
Figure 4: Evaluation of Retail Banking Services by CRA Examination Type 23
Figure 5: Evaluation of Small-Dollar, Nonmortgage Consumer Loans by CRA Examination Type 25
Figure 6: Evaluation of Support for Community Development by CRA Examination Type 26

Abbreviations

AFS	alternative financial services
APR	annual percentage rate
ATM	automated teller machine
CDFI	community development financial institution
Census	Census Bureau
CFPB	Consumer Financial Protection Bureau
CRA	Community Reinvestment Act
CPS	Current Population Survey
FDIC	Federal Deposit Insurance Corporation
FFIEC	Federal Financial Institutions Examination Council
fintech	financial technology
FRB	Board of Governors of the Federal Reserve System
LMI	low and moderate income
NAICS	North American Industry Classification System
NCUA	National Credit Union Administration
OCC	Office of the Comptroller of the Currency
Q&A	Interagency Questions and Answers
Treasury	Department of the Treasury

This is a work of the U.S. government and is not subject to copyright protection in the United States. The published product may be reproduced and distributed in its entirety without further permission from GAO. However, because this work may contain copyrighted images or other material, permission from the copyright holder may be necessary if you wish to reproduce this material separately.

U.S. GOVERNMENT ACCOUNTABILITY OFFICE

441 G St. N.W.
Washington, DC 20548

February 14, 2018

The Honorable Elizabeth Warren
Ranking Member
Subcommittee on Financial Institutions and Consumer Protection
Committee on Banking, Housing, and Urban Affairs
United States Senate

The Honorable Elijah E. Cummings
Ranking Member
Committee on Oversight and Government Reform
House of Representatives

While the percentage of unbanked U.S. households—those without a checking or savings account—had fallen since 2011 (to about 7 percent), about 20 percent of U.S. households (or about 51 million adults) remained underbanked in 2015.[1] These underbanked households had a bank account but still relied on alternative financial services (AFS) providers for basic banking services like check cashing or small-dollar, nonmortgage consumer loans.[2] The Community Reinvestment Act (CRA), which was enacted in 1977, is intended to encourage financial institutions to help meet the credit needs of the communities in which they operate, including low- and moderate-income (LMI) neighborhoods, consistent with safe and sound banking operations. CRA encourages financial institutions to provide a wide variety of options to serve the needs of their communities, including mortgage, consumer, and business lending; community investments; and low-cost services that would benefit LMI areas and individuals. CRA's implementation is overseen by the federal banking regulators—the Board of Governors of the Federal Reserve System (FRB), Federal Deposit Insurance Corporation (FDIC), and Office of the Comptroller of the Currency (OCC).

Some groups have argued that revisions to CRA could further encourage institutions to serve the unmet banking service and small-dollar credit

---

[1]See Federal Deposit Insurance Corporation, *2015 FDIC National Survey of Unbanked and Underbanked Households* (Washington, D.C.: Oct. 20, 2016).

[2]AFS providers include transaction providers such as check cashing outlets and money transmitters and credit providers such as payday loan stores, automobile title lenders, and pawnshop lenders. AFS providers operate outside of federally insured banks, credit unions, and thrifts.

needs of LMI communities. In June 2017, the Department of the Treasury (Treasury) issued a report noting, among other things, the need to modernize outdated statutes and regulations, including CRA, to conform to the realities of the current financial system.[3] For example, Treasury noted the supervisory and regulatory framework for CRA, including the examination process and rating system, need to reflect the variety of ways banks currently do business and meet the needs of diverse consumers and communities.

You asked us to assess financial institutions' provision of basic banking services and small-dollar, nonmortgage consumer loans in LMI communities, including CRA's role in doing so. You also asked us to evaluate how financial institutions' support for community development is assessed during the CRA examination process. Specifically, this report examines: (1) the availability of financial products and services to LMI consumers and their use of such products and services; (2) the extent to which CRA examinations evaluate financial institutions' provision of retail banking services, small-dollar, nonmortgage consumer loans, and support for community development in LMI communities; and (3) stakeholder views on options that could further encourage services and loans in LMI communities.[4]

To address our objectives, we reviewed the CRA statute and related regulations and interviewed FRB, FDIC, and OCC officials. To assess the extent to which financial products and services are available to LMI consumers and their use of such products and services, we used, among other things, 2016 data from the Census Bureau (Census), FDIC, and the National Credit Union Administration (NCUA) to estimate how the availability of basic banking services offered by banks, credit unions, and AFS providers in LMI communities compares to that in other communities. In addition, we analyzed FDIC's National Survey of Unbanked and Underbanked Households data for 2011, 2013, and 2015 to estimate the relationship between household income and various financial behaviors and characteristics of households related to the use and accessibility of basic banking services and small-dollar loans. We reviewed documentation on and conducted testing of the data we used

[3]See U.S. Department of the Treasury, *A Financial System That Creates Economic Opportunities: Banks and Credit Unions* (Washington, D.C.: June 2017).

[4]Basic banking services are a subset of retail banking services, which is the term used in the CRA regulations and examination procedures.

and determined they were sufficiently reliable for the purpose of reporting on consumers' access to financial institutions and AFS providers as well as on how consumers' use of financial products and services vary with income.

To determine the extent to which CRA examinations evaluate financial institutions' provision of retail banking services; small-dollar, nonmortgage consumer loans; and support for community development in LMI communities, we reviewed a representative random sample of 219 CRA performance evaluations stratified by the examination type—large, intermediate small, and small bank examinations. Our sampling frame includes all 1,273 CRA evaluations of large, intermediate small, and small institutions that were conducted in calendar year 2015 and published by July 19, 2016. The final sample included 59 large, 76 intermediate small, and 84 small bank examinations. Using data collection instruments developed by reviewing CRA examination procedures for the three examination types, we analyzed this sample of reports to determine the extent to which they included evaluations of financial institutions' provision of retail banking services; small-dollar, nonmortgage consumer loans; and support for community development in LMI communities. We also interviewed representatives of five financial institutions with 2015 CRA performance evaluations that mentioned consumer loans and the CRA examiners who conducted these evaluations to determine how those loans were evaluated under CRA.

To determine stakeholder views on options that could further encourage services and loans in LMI communities, we conducted a literature review of scholarly studies, policy briefs, news articles, and other sources. We also held a series of interviews with 16 stakeholders—including representatives of government agencies, industry associations, think tanks, and consumer advocacy organizations—to identify options that could encourage financial institutions to provide such services and loans. We analyzed and grouped the list of suggested options identified in literature and interviews. To obtain information on the relative importance of these suggested options, we sent a survey to 66 stakeholders (individuals and organizations). We then held a series of discussion groups with representatives of the federal banking regulators and others who responded to our survey to obtain their views on the suggested options. (See app. I for a detailed description of our scope and methodology.)

We conducted this performance audit from August 2015 through February 2018 in accordance with generally accepted government auditing

standards. Those standards require that we plan and perform the audit to obtain sufficient, appropriate evidence to provide a reasonable basis for our findings and conclusions based on our audit objectives. We believe that the evidence obtained provides a reasonable basis for our findings and conclusions based on our audit objectives.

Background

Community Reinvestment Act

Congress passed CRA in 1977 to encourage banking institutions to meet the credit needs of the communities in which they operate, including LMI neighborhoods, consistent with safe and sound banking operations.[5] To do so, CRA requires federal banking regulators to conduct examinations to regularly assess the records of financial institutions in terms of meeting local credit needs and issue performance ratings. CRA regulations use data on family income in a census tract relative to family income in the surrounding metropolitan area or nonmetropolitan (henceforth, rural) area of the state where the tract is located to determine LMI communities. A census tract is low income if median family income in the tract is less than 50 percent of the median family income in the surrounding metropolitan area or rural area, and it is moderate income if median family income in the tract is at least 50 percent and less than 80 percent of median family income in the surrounding metropolitan area or rural area. For example, in 2017, median family income in the Baltimore-Columbia-Towson metropolitan area was about $91,100. Therefore, moderate-income tracts in this metropolitan area were those with median family income of at least $45,550 but less than $72,880, while low-income tracts were those with median family income less than $45,550.

CRA was amended in 1989 to require public disclosure of portions of CRA reports, including ratings, and to require CRA examinations to have a four-tiered system of descriptive performance levels (Outstanding, Satisfactory, Needs to Improve, or Substantial Noncompliance). In 1995, the CRA examination was customized to account for differences in institution sizes and business models, with different examination procedures defined for small and large institutions. In 2005, the institution size definitions were revised to include intermediate small institutions and

[5]Pub. L. No. 95-128, title VIII, 91 Stat.1111,1147 (1977), codified, as amended, at 12 U.S.C. §§2901-2908.

were indexed to the Consumer Price Index.[6] In addition, CRA has evolved to include a greater emphasis on consumer and business lending, community investments, and low-cost services that would benefit LMI areas and individuals.

CRA applies to regulated financial institutions (insured depository institutions) such as national banks, savings associations, and state-chartered commercial and savings banks, but does not apply to credit unions and nonbanks, such as insurance companies, securities companies, and others. Therefore, CRA is implemented by the federal banking regulators—FRB, FDIC, and OCC.[7] The three federal banking regulators work together to promote consistency in the implementation of the CRA regulations by providing guidance on the interpretation and implementation of the CRA regulations through *Interagency Questions and Answers Regarding Community Reinvestment* (CRA Q&A) and examination procedures and by facilitating uniform data reporting. In addition, the federal banking regulators work through the Federal Financial Institutions Examination Council (FFIEC) to periodically publish the CRA Q&As and examination procedures and to facilitate the release of uniform data reporting to the public.[8] The federal banking regulators conduct periodic examinations to evaluate how banks are fulfilling the objectives of CRA in their designated assessment areas and issue performance ratings as listed above. Institutions desire a satisfactory or

---

[6]CRA institution size thresholds are indexed to the Consumer Price Index, which is calculated by the Bureau of Labor Statistics and is the principal measure of trends in consumer prices and inflation in the United States. As of January 1, 2018, a “small institution” was defined as having less than $1.252 billion in assets, an “intermediate small institution” (a subset of “small institutions”) had at least $313 million but less than $1.252 billion, and a “large institution” had $1.252 billion or more in assets.

[7]FRB regulates state banks that are members of the Federal Reserve System, state-chartered U.S. branches of foreign banks, and foreign branches of U.S. banks. OCC regulates national banks, U.S. federal branches of foreign banks, and federally-chartered thrift institutions. FDIC regulates state-chartered banks and savings institutions that are not members of the Federal Reserve System.

[8]FFIEC is a formal interagency body that works to prescribe uniform principles, standards, and report forms for the federal examination of financial institutions and to make recommendations to promote uniformity in the supervision of financial institutions. In addition to FRB, FDIC, and OCC, FFIEC members include NCUA, which provides regulation and oversight supervision for credit unions in the U.S., and the Consumer Financial Protection Bureau (CFPB), which enforces federal consumer financial laws and protects consumers in the financial marketplace. Additionally, FFIEC includes a State Liaison Committee composed of five representatives of state supervisory agencies. The State Liaison Committee Chairman is a voting member of FFIEC.

better CRA rating, as it is considered when they apply to their regulators for new branches, mergers, and acquisitions and submit other applications that require regulatory approval. According to FRB officials, the public nature of ratings can also provide an incentive for banks to achieve a Satisfactory or better rating.

Institutions designate one or more assessment areas for CRA purposes. These assessment areas must include the locations of the institution's main office, branches, and deposit-taking automated teller machines (ATM), as well as the surrounding geographies where the institution has originated or purchased a substantial portion of its loans. To determine an institution's rating, the federal banking regulators apply a selection of component tests, depending on institution size. Large institutions are subject to the lending test, investment test, and service test. Intermediate small institutions are subject to the lending test and the community development test. Small institutions are subject to the lending test, and may opt to have their qualified investments and services reviewed to enhance a "Satisfactory" rating.[9] These CRA tests are described below:

- The **lending test** evaluates the number, amount, and distribution across income and geographic classifications of the institution's home mortgage, small business, small farm, and consumer loans in the assessment area.[10] Depending on the size of the institution, the lending test may also include evaluation of the institution's community

[9]Under CRA regulations, an institution may apply to its primary federal banking regulator to be designated a *limited purpose* or *wholesale* bank. Such institutions are evaluated for performance under separate standards. A *limited purpose bank* is a bank that offers a narrow product line (such as credit card or motor vehicle loans) to a regional or broader market. A *wholesale bank* is a bank that does not extend home mortgage, small business, small farm, or consumer loans to retail customers. In addition, under CRA an institution may apply to its primary federal banking regulator to be evaluated under a *strategic plan* instead of the CRA regulation. The plan must address all three CRA performance categories (lending, investment, and services), but the institution may tailor its CRA objectives to the needs of the community and to its own capacities, business strategies, and expertise.

[10]CRA was enacted, in part, in response to concerns about redlining, or banks' refusal to offer home loans in certain neighborhoods based on the income or racial composition of the area. Because home mortgages comprise a substantial majority of many financial institutions' lending portfolios, they are often a key component of CRA reviews.

development loans and any innovative or flexible loan products. This test has the greatest effect on a large institution's overall rating.[11]

- The **investment test** grades the dollar amount, complexity, and responsiveness of qualified community development investments that benefit the institution's assessment area(s) or a broader statewide or regional area that includes the institution's assessment area(s). These are investments, grants, or deposits that generally serve LMI individuals and areas.
- The **community development test** assesses the institution's community development loans, investments, and services, as appropriate. Under CRA, qualifying community development activities may be related to: affordable housing for LMI individuals; community services targeted to LMI individuals; economic development through financing small businesses or small farms; and stabilization or revitalization of LMI communities, designated disaster areas, or distressed or underserved middle-income communities as designated by FRB, FDIC, or OCC.
- The **service test** examines retail service delivery, such as the availability and accessibility of branches, products, and alternative delivery systems like ATMs and mobile banking in the assessment area and across income levels. The service test also evaluates the extent, innovativeness, and responsiveness of the institution's community development services.

When applying these tests, the federal banking regulators consider the institution's performance relative to demographic data; institutional capacity and constraints; and lending, investment, and service opportunities in the institution's assessment area, known as the performance context.

Basic Banking Services and Small-Dollar Loans

Basic banking services refers to those financial services needed to allow the average consumer to engage in necessary day-to-day banking activities. These services include deposit taking and simple transaction or savings account programs with low fees. While there is no single, universal definition of small-dollar loans, the term generally refers to

[11]For intermediate small institutions, the lending and community development tests are weighted equally. An intermediate small institution must receive a satisfactory rating on both tests to receive a satisfactory rating overall.

unsecured, nonmortgage consumer loans that are less than $2,500. These loans may include various fees, interest rates, and terms.

A payday loan is generally defined as a single payment, short-term loan based on a personal check held for future deposit or electronic access to a personal checking account. Payday loans can be approved within minutes, and the typical loan is for $100–$500 and a 14-day term. However, payday and similar loans have been criticized for their often triple-digit annual percentage rates (APR) and the frequency with which cash-constrained borrowers roll over or take out successive loans rather than repay the original principal amount in full when due.[12] For example, we found in January 2011 that payday loans were generally priced at a fixed-dollar fee ranging from $15–$20 per $100 borrowed, which was equivalent to an APR of 300–600 percent.[13] We noted that if a borrower was unable to repay the loan on the due date, the borrower generally could pay an additional fee to extend ("roll over") the loan—for example, for another 2 weeks. We also concluded that if borrowers extended a loan multiple times or obtained consecutive loans, the payday loan cycle could continue for weeks or months, costing the borrower much more than the initial amount borrowed. The Pew Charitable Trusts reported in 2012 that payday loan borrowers were actually indebted for an average of 5 months per year, and that on average, a borrower took out eight loans of $375 each per year (or rolled the same loan over multiple times) and spent $520 on interest.[14]

Banks and credit unions offer some products that may be seen as alternatives to payday loans, such as small-dollar consumer loans and overdraft services. FDIC found in a 2011 survey of banks' efforts to serve the unbanked and underbanked that about 43 percent of banks had developed a range of products and services specifically for underserved

[12]See Susanna Montezemolo, *Payday Lending Abuses and Predatory Practices* (Durham, NC: Center for Responsible Lending, September 2013). This chapter was part of a larger report, *The State of Lending in America & its Impact on U.S. Households*, accessed on November 30, 2017, and is available at http://www.responsiblelending.org/state-of-lending/reports/10-Payday-Loans.pdf.

[13]GAO, *Payday Lending: Federal Law Enforcement Uses a Multilayered Approach to Identify Employees in Financial Distress,* GAO-11-147 (Washington, D.C.: Jan. 26, 2011).

[14]The Pew Charitable Trusts, *Payday Lending in America: Who Borrows, Where They Borrow, and Why* (Washington, D.C.: July 2012).

consumers.[15] The survey also found that 82 percent of all banks reported offering unsecured personal loans with no minimum loan amount or a minimum loan amount of $2,500 or less.[16] Consumers may also use overdraft services as a source of short-term credit. According to CFPB, overdrafts occur when a debit transaction (payment or withdrawal) exceeds the consumer's account balance.[17] For a fee, the bank will cover these transactions and collect the funds, including all associated fees, from the consumer's next deposit into the account. However, consumers must have an established account with the bank to qualify for this product, and high fees can make this a costly form of short-term credit.[18]

Number of Bank and Credit Union Branches and AFS Providers

The number of bank and credit union branches and AFS establishments nationwide has decreased overall in recent years (see fig. 1). The number of bank branches in the U.S. generally rose steadily from 2005 to 2009, but has decreased each year since then, from 98,943 in 2009 to 91,445 in 2016—about the number of branches in the U.S. in 2005. Similarly, the number of credit union branches nationwide has decreased from 22,728 in 2011 (the earliest year for which data were available) to 21,733 branches in 2016.[19] The number of AFS establishments in the U.S. has fluctuated, but decreased overall from 32,243 establishments in 2009 to 30,396 in 2015 (the most recent year for which data were available).

[15]Federal Deposit Insurance Corporation, *2011 FDIC Survey of Banks' Efforts to Serve the Unbanked and Underbanked* (Washington, D.C.: December 2012).

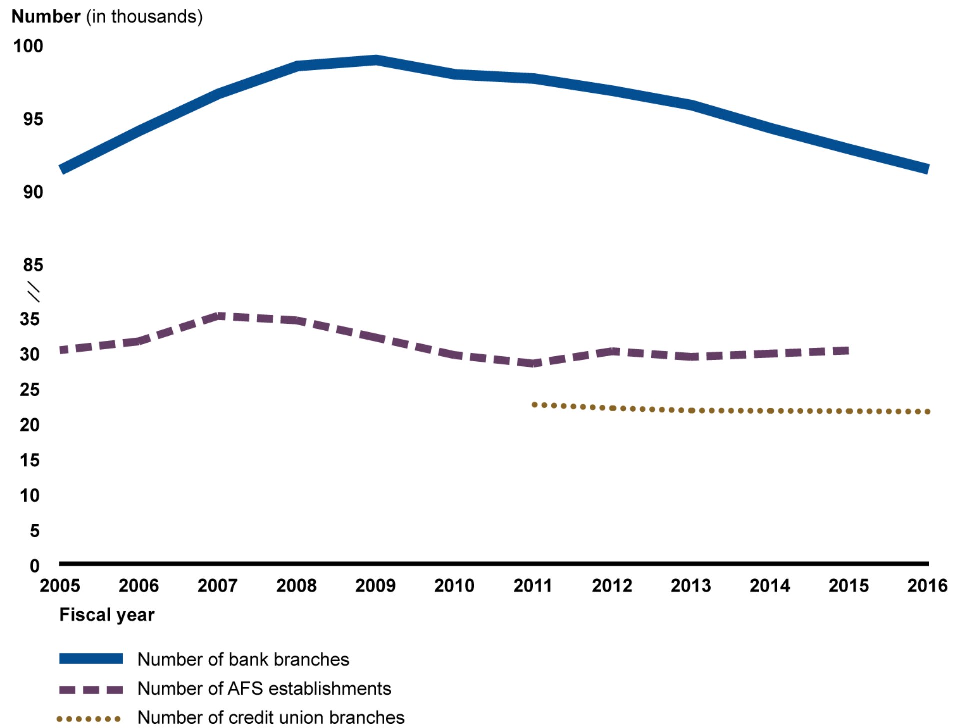
[16]FDIC conducted a small-dollar loan pilot program from 2007 through 2009 designed to illustrate how banks can profitably offer affordable small-dollar loans as an alternative to high-cost credit products such as payday loans and fee-based overdraft programs. The pilot program resulted in a template for small-dollar loans: low- or no-fee loans of $2,500 or less, with a term of 90 days or more, an APR of 36 percent or less, and a streamlined underwriting system enabling banks to issue a loan decision within 24 hours of a loan application. See Federal Deposit Insurance Corporation, "A Template for Success: The FDIC's Small-Dollar Loan Pilot Program," *FDIC Quarterly*, vol. 4, no. 2 (Washington, D.C.: 2010).

[17]Consumer Financial Protection Bureau, *CFPB Study of Overdraft Programs: A white paper of initial data findings* (Washington, D.C.: June 2013).

[18]Consumer Financial Protection Bureau Regulation E, which implements the Electronic Fund Transfer Act, requires depository institutions to provide notice and a reasonable opportunity for customers to opt in to overdraft protection for ATM and most debit card transactions. 15 U.S.C. § 1693 et seq.; Regulation E, 12 C.F.R. part 1005.

[19]Changes in the numbers of bank and credit union branches can be the result of changes in the numbers of banks and credit unions, as well as changes in the numbers of branches for each active bank and credit union.

Figure 1: Number of Bank Branches, Credit Union Branches, and Alternative Financial Services (AFS) Establishments Nationwide, 2005 through 2016



Source: GAO analysis of Federal Deposit Insurance Corporation, National Credit Union Administration, and Census data. | GAO-18-244

Note: Credit union branch data were not available for years prior to 2011.

Financial Services Providers' Availability to Lower-Income Consumers Varies by Location, and Lower-Income Consumers Are More Likely to Use Alternative Providers

On the basis of our econometric analysis, we found that LMI communities have at least as many banks, credit unions, and AFS providers nearby as middle-income communities in some areas but less in others. In addition, our analysis of recent survey data suggests lower-income households were more likely to obtain credit or conduct financial transactions through an AFS provider and less likely to have a checking or savings account with a bank or credit union than their higher-income counterparts. Further, lower-income households were more likely to be unbanked because they lacked sufficient funds, credit, or personal identification.

Availability of Banks, Credit Unions, and AFS Providers to LMI Communities Varies by Location

Our econometric analysis of recent FDIC, FFIEC, NCUA, and Census data found that LMI census tracts (referred to throughout this report as "communities") generally have at least as many banks and credit unions nearby as middle-income communities in rural areas and most metropolitan areas, but have fewer nearby in smaller metropolitan areas.[20] We found that low-income communities in rural areas and in metropolitan areas with at least 100,000 people have at least as many bank and credit union branches (referred to collectively throughout this report as "branches") within 2 miles as middle-income communities, all else being equal, but low-income communities in metropolitan areas of less than 100,000 people have fewer branches within 2 miles than middle-income communities.[21] For example, we estimated that low-income communities in metropolitan areas with 250,000 to 499,999 people have about 11 percent more branches within 2 miles than similar middle-income communities (see table 1). We also estimated that low-income communities in metropolitan areas with 500,000 to 999,999 have about 22 percent more branches within 2 miles than similar middle-income communities in the same area, and those in metropolitan areas with 1 million people or more have about 31 percent more. However, we

[20]For this analysis, we used 2010 and 2016 data from Census and 2016 data from FFIEC, FDIC, and NCUA to analyze the availability of financial services providers by counting the number of bank and credit union branches within 2, 5, and 10 miles of the central point of a census tract, or community. We analyzed census tracts, or communities, based on income level with an emphasis on LMI communities. The econometric analysis includes several control variables, such as tract income; population density and land use category; the demographic mix of tract population by age, race/ethnicity, gender, educational attainment, and labor force status; and the mix of homes by homeownership status. Our analysis is subject to limitations. For example, the results of our analysis may not generalize to other time periods. In addition, our results are indicative of the availability of basic banking services for LMI communities on average, but availability for a specific LMI community may be different. Similarly, availability of banks may differ from that of credit unions. There may be alternative measures of availability other than the numbers of branches within a given distance from a census tract, and these measures may produce different results. Although we controlled for several important drivers of differences in the number of bank and credit union branches across communities, our work does not establish causal relationships between community income and availability of basic banking services. Finally, proximity to providers of banking services is only one type of availability, and LMI communities may face other barriers to accessing banking services. See appendix II for more details about our analysis and findings.

[21]Our analysis indicated similar patterns when examining the number of branches at distances greater than 2 miles from the center of a community. In general, LMI communities in rural areas and metropolitan areas of all sizes had at least as many branches within 5 and 10 miles as similar middle-income communities. See appendix II for more details about our analysis and findings.

estimated that low-income communities in rural areas and in metropolitan areas with 100,000 to 249,000 people have about the same number of branches within 2 miles as middle-income communities, and those in metropolitan areas with less than 100,000 people have about 35 percent fewer. We found that moderate-income communities in rural areas and metropolitan areas of all sizes have at least as many branches within 2 miles as middle-income communities, all else being equal.

Table 1: Estimated Differences in Number of Bank and Credit Union Branches Nearby Low- and Moderate-Income Communities Relative to Middle-Income Communities, by Location Type, 2016

(percent)

	Estimated percent difference between the number of bank and credit union branches within 2 miles of low- and moderate-income communities and the number within 2 miles of similar middle-income communities in					
	rural areas	metropolitan areas with				
Community income		99,999 people or fewer	100,000 to 249,999 people	250,000 to 499,999 people	500,000 to 999,999 people	1 million people or more
Low	No significant difference	-35	No significant difference	+11	+22	+31
Moderate	No significant difference	No significant difference	+7	+10	+10	+10

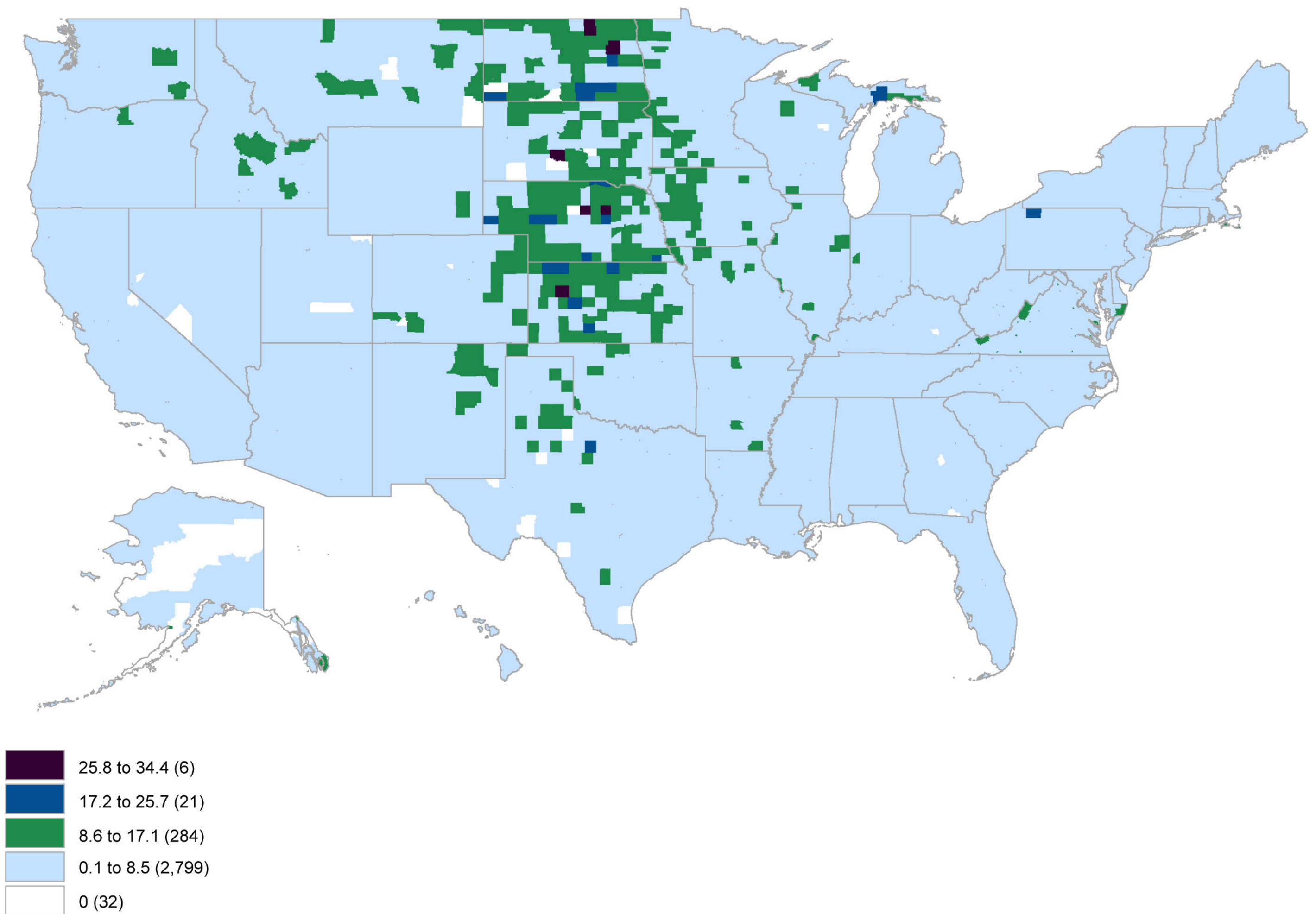
Source: GAO analysis of data from the Census Bureau, the Federal Deposit Insurance Corporation, the Federal Financial Institutions Examination Council, and the National Credit Union Administration. | GAO-18-244

Notes: The table shows the estimated average percent difference between the numbers of bank and credit union branches within 2 miles of low- and moderate-income communities and the number within 2 miles of similar middle-income communities in the same metropolitan area or rural area. These averages were estimated using regressions that also controlled for community population density and land use; the demographic mix of people in the community by age, race/ethnicity, gender, educational attainment, and labor force status; the mix of homes in the community by homeownership status; and the metropolitan area or rural area of the state where the community is located. All estimates are statistically significant at the 5 percent level or better unless otherwise noted. See appendix II for the details of our analysis and table 13 in appendix II for more information about these results.

At the same time, our analysis of recent Census data also suggests that the number of branches nearby communities of all income levels varies across the country. We found that the number of branches per 10,000 people in a county was generally higher in the Midwest than the number in other regions in 2016 (see fig. 2). Most U.S. counties had no more than about 9 branches per 10,000 people, and only 32 counties had no branches. However, many counties in the Midwest had more than about 9 branches per 10,000 people, and some had more than 17 branches per 10,000 people. Thus, while the number of branches nearby LMI communities may be similar to or greater than the number of branches nearby middle-income communities in the same metropolitan area or rural

area of a state, the number of branches nearby LMI communities in different parts of the country may be quite different.

Figure 2: Numbers of Bank and Credit Union Branches per 10,000 People by County, 2016 (number of counties)



Source: GAO analysis; MapInfo (map). | GAO-18-244

Our analysis of the availability of AFS providers, such as payday lenders and check cashers, to LMI communities found that counties with a higher proportion of residents in LMI communities generally do not have more

AFS establishments and, in fact, may have fewer in some areas.[22] These findings were generally consistent with the results of other studies on the topic.[23] For example, a 2014 study found that if anything, the numbers of certain AFS establishments—specifically, payday loan stores, pawnshops, and check cashers—per capita are smaller in counties with more people with income below the poverty line, all else being equal.[24]

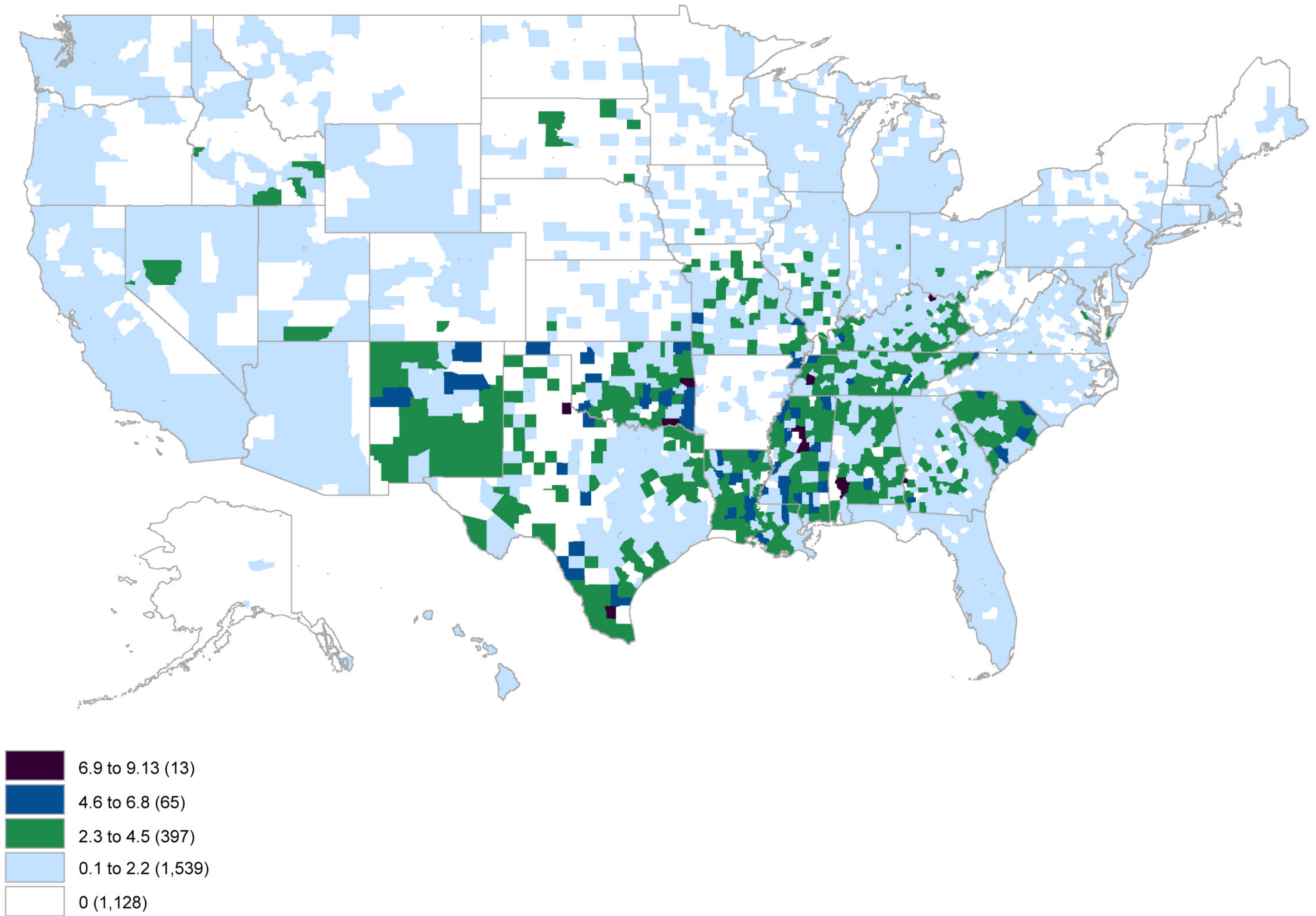
At the same time, our analysis of recent Census data found that the number of AFS establishments nearby communities of all income levels varies across the country. We found that the number of AFS establishments per 10,000 people in a county was generally higher in the South than the number in other regions in 2016 (see fig. 3). Most U.S. counties had no more than about 2 AFS establishments per 10,000 people, and 1,128 counties had no AFS establishments. However, many counties in the South had more than 2 AFS establishments per 10,000 people, and some had more than 5 AFS establishments per 10,000 people. Thus, while the number of AFS establishments nearby LMI communities may be comparable to the number nearby middle-income communities in the same metropolitan area or rural area of a state, the number of AFS establishments nearby LMI communities in different parts of the country may be quite different.

[22]According to the National Conference of State Legislatures, some states prohibit payday lending. However, other types of AFS establishments may still operate. In 2014 in states that do not prohibit payday lending, there were generally fewer AFS establishments in counties with more residents in low-income communities. Specifically, a 1 percentage point increase in the share of residents in low-income communities was associated with about a 1 percent reduction in the number of AFS establishments in a county, all else being equal. In states that do prohibit payday lending, the number of AFS establishments in a county was unrelated to the share of people living in low-income communities. Similarly, the number of AFS establishments in a county was not associated with the number of residents in moderate-income communities, regardless of whether a state prohibits payday lending.

[23]We analyzed county-level data on the proportion of a county's residents who live in low- or moderate-income communities and the number of AFS establishments located in the county. We used 2014 county data from Census and FFIEC. This analysis controlled for several relevant factors, such as the distribution of county population across different groups by race, gender, age, education, and employment status. See appendix II for a more in-depth discussion of our analysis and findings.

[24]R. A. Prager, "Determinants of the Locations of Alternative Financial Service Providers," *Review of Industrial Organization*, vol. 45, no. 1 (2014).

Figure 3: Number of Alternative Financial Services Establishments per 10,000 People by County, 2016 (number of counties)



Source: GAO analysis; MapInfo (map). | GAO-18-244

Lower-Income Households Are Less Likely to Use Banks and Credit Unions Than Higher-Income Households

Despite the availability of bank and credit union branches, our econometric analysis of 2015 National Survey of Unbanked and Underbanked Households data suggests that lower-income households were generally less likely to access products and services and conduct transactions through banks and credit unions than higher-income households.[25] We estimated that 7 percent of households were unbanked, or did not have a checking or savings account, and lower-income households were more likely to be unbanked than higher-income households.[26] For example, we estimated that, in 2015, the share of households with income less than $15,000 that had a checking or savings account was about 15.1 percentage points lower than the share of similar households with income of $75,000 or more that had a checking or savings account, and the share of households with income from $15,000 to $29,999 that had a checking or savings account was about 4.5 percentage points lower (see table 2). A 2016 study reported similar results, finding that lower-income households were less likely to have a bank account.[27] We also found that households with lower incomes were less likely to receive income and pay bills through bank-associated methods such as online transfers and bill pay, and they were less likely to have direct deposit.[28]

---

[25]Federal Deposit Insurance Corporation, *2015 FDIC National Survey of Unbanked and Underbanked Households*. See appendix III for additional information about this analysis.

[26]Our analysis controlled for several variables, such as family type, primary language, age, education, employment status, citizenship status, and race. Our analysis is subject to limitations. For example, our results may not generalize to other time periods. In addition, our results are indicative of the experience of households on average, but the experience of an individual household may differ. Furthermore, the data do not include variables identifying households' locations at levels of detail more fine than the metropolitan area in which they live. Thus, we are not able to account for the characteristics of a household's local community that may influence their decisions, such as the numbers of banks and AFS providers nearby.

[27]R. M. Goodstein and S. L. W. Rhine, "The Effects of Bank and Nonbank Provider Locations on Household Use of Financial Transaction Services," *Journal of Banking and Finance*, vol. 78, no. 5 (2017).

[28]Our analysis also demonstrated that income is not the only factor that affects consumer choices about services and loans; other characteristics, such as homeownership, are factors that affect choices about accessing basic banking services and small-dollar, unsecured loans. See appendix III for a more in-depth discussion of our analysis and findings.

Table 2: Estimated Differences in Use of Banks and Credit Unions by Lower-Income Households Relative to Households with Annual Income of $75,000 or More, 2015

(percentage points)

Household annual income	Estimated difference between the percentage of lower-income households and the percentage of similar households with annual income of $75,000 or more that: had a checking or savings account	typically received income and paid bills using methods associated with banks in the preceding year	used direct deposit in the preceding year
Less than $15,000	-15.1	-21.3	-23.2
$15,000 to $29,999	-4.5	-14.3	-14.8
$30,000 to $49,999	No significant difference	-8.2	-7.9
$50,000 to $74,999	+1.1	-4.5	-2.9

Source: GAO analysis of data from the Federal Deposit Insurance Corporation. | GAO-18-244

Notes: The table shows the estimated average difference between (1) the percentage of households with income in a given lower range using a basic banking service and (2) the percentage of similar households in the same metropolitan area or rural area with income of $75,000 or more using that service. These differences were estimated using regressions that also control for family type, homeownership, and language spoken at home, as well as the age, education, labor force status, nativity and citizenship, and race/ethnicity of the head of the household, and the location type and metropolitan area or state rural area where the household is located. All estimates are statistically significant at the 5 percent level or better unless otherwise noted. See appendix III for the details of our analysis and see table 20 in appendix III for more information about these results.

Our analysis of 2015 National Survey of Unbanked and Underbanked Households data also suggests that lower-income households can have different reasons for being unbanked—not having a checking or savings account—than higher-income households.[29] Among unbanked households, lower-income households were more likely to say that they were unbanked because they did not have enough money to keep in an account or because they had personal identification, credit, or former bank account problems. For example, compared to the share of households with income of $75,000 or more citing not having enough money to keep in an account as a reason for being unbanked, we estimated that the share of households with income between $30,000 and $49,999 citing that reason was about 19 percentage points higher, the share of households with income between $15,000 and $29,999 citing

[29]We analyzed data from FDIC's National Survey of Unbanked and Underbanked Households to estimate the relationship between household income and various financial behaviors and characteristics of households related to the use and accessibility of basic banking services and small-dollar loans. (For technical details on our household analysis, see app. III.)

that reason was about 27 percentage points higher, and the share of households with income less than $15,000 citing that reason was about 34 percentage points higher. Households with incomes between $30,000 and $74,999 were more likely than other households to be unbanked because bank hours or locations were inconvenient. Among unbanked households, those with lower incomes were just as likely as those with higher incomes to cite high or unpredictable bank fees, among other reasons, as the reason they were unbanked.

Lower-Income Households Are More Likely to Use AFS Providers Than Higher-Income Households

Our analysis of 2015 National Survey of Unbanked and Underbanked Households data found that lower-income households were more likely to obtain credit or engage in financial transactions through an AFS provider than their higher-income counterparts. Overall, we estimated that about 20 percent of households reported using AFS providers for transactions in the past year, and about 8 percent reported using nonbank or AFS providers for credit. Households with less than $75,000 in income were more likely than those with higher incomes to report using an AFS provider in the past 12 months for transactions and for credit. For example, we estimated that the share of households with income less than $15,000 that used AFS providers for transactions was about 11 percentage points higher than the share of households with income of $75,000 or more that did so, and the share of households with income less than $15,000 that used AFS providers for credit was about 4 percentage points higher (see table 3). Other research has also found that lower-income consumers are more likely to use AFS providers. The Pew Charitable Trusts reported in 2012 that 12 million people took out payday loans each year, and about 5.5 percent of American adults had used a payday loan in the past 5 years.[30] CFPB reported in 2013 that 84 percent of payday loan borrowers had a reported annual income of less than $40,000; 43 percent of borrowers had a reported income of less than $20,000 annually.[31]

[30]The Pew Charitable Trusts, *Payday Lending in America: Who Borrows, Where They Borrow, and Why*.

[31]Consumer Financial Protection Bureau, *Payday Loans and Deposit Advance Products: A White Paper of Initial Data Findings* (Washington, D.C.: Apr. 24, 2013).

Table 3: Estimated Differences in Use of Alternative Financial Services Providers by Lower-Income Households Relative to Households with Annual Income of $75,000 or More, 2015

(percentage points)

	Estimated difference between the percentage of lower-income households and the percentage of similar households with annual income of $75,000 or more that:	
Household annual income	**used AFS providers for transactions**	**obtained credit from AFS providers**
Less than $15,000	+11.0	+3.9
$15,000 to $29,999	+7.4	+3.5
$30,000 to $49,999	+4.4	+3.6
$50,000 to $74,999	+3.0	+1.5

Source: GAO analysis of data from the Federal Deposit Insurance Corporation. | GAO-18-244

Notes: The table shows the estimated average difference between (1) the percentage of households with income in a given lower range using alternative financial services providers and (2) the percentage of similar households in the same metropolitan area or rural area with income of $75,000 or more using alternative financial services providers. These differences were estimated using regressions that also control for family type, homeownership, and language spoken at home, as well as the age, education, labor force status, nativity and citizenship, and race/ethnicity of the head of the household, and the location type and metropolitan area or state rural area where the household is located. All estimates are statistically significant at the 5 percent level or better unless otherwise noted. See appendix III for the details of our analysis and see tables 20 and 23 in appendix III for more information about these results.

Our analysis suggests that lower-income households may have greater demand for small-dollar loans than their higher-income counterparts, but are more likely to obtain them from AFS providers. We found that households with lower incomes were less likely than similar households with higher incomes to have saved for unexpected expenses and more likely to have fallen behind on bills (see table 4). However, lower-income households were less likely to have had consumer credit from a bank, and more likely to report being credit constrained, meaning they were unable to obtain credit or discouraged from applying for credit from a bank.

Table 4: Estimated Differences in Saving, Bill-Paying, and Consumer Credit Behaviors for Lower-Income Households Relative to Households with Annual Income of $75,000 or More, 2015

(percentage points)

	Estimated difference between the percentage of lower-income households and the percentage of similar households with annual income of $75,000 or more that:			
Household annual income	**set aside money for unexpected expenses or emergencies**	**fell behind on bills**	**had consumer credit from a bank**	**were consumer credit constrained**
Less than $15,000	-27.4	+18.5	-5.9	+3.1
$15,000 to $29,999	-19.1	+14.0	-4.5	+3.7
$30,000 to $49,999	-12.0	+8.6	-3.2	+2.0
$50,000 to $74,999	-6.0	+4.9	-2.1	+1.6

Source: GAO analysis of data from the Federal Deposit Insurance Corporation. | GAO-18-244

Notes: The table shows the estimated average difference between (1) the percentage of households with income in a given lower range that exhibited a behavior and (2) the percentage of similar households in the same metropolitan area or rural area with income of $75,000 or more that exhibited the same behavior. These differences were estimated using regressions that also control for family type, homeownership, and language spoken at home, as well as the age, education, labor force status, nativity and citizenship, and race/ethnicity of the head of the household, and the location type and metropolitan area or state rural area where the household is located. All estimates are statistically significant at the 5 percent level or better unless otherwise noted. See appendix III for the details of our analysis and see table 23 in appendix III for more information about these results.

While Limited for Certain Institutions, Scope of CRA Evaluations Was Consistent with Examination Procedures

CRA examinations do not always evaluate financial institutions' provision of retail banking services, small-dollar, nonmortgage consumer lending, or support for community development in LMI areas because such assessments are not required for every institution.[32] Our review of a representative random sample of 219 CRA public disclosure performance evaluations (performance evaluations) for examinations conducted in 2015 found that evaluations of retail banking services, small-dollar nonmortgage consumer lending, and support for community development in LMI areas varied across examination types.[33] For example, while larger institutions are subject to evaluations of their services, lending, and support of community development, smaller institutions are primarily evaluated on their lending. Further, in line with CRA's primary focus on home mortgage, small business, and small farm loans—loans that tend to comprise the bulk of financial institutions' portfolios—CRA examinations typically only evaluate a financial institution's consumer lending if it is a substantial majority of the institution's lending or a major product line, which generally is not the case across all institution types.

[32]As noted previously, basic banking services are a subset of retail banking services, which is the term used in the CRA regulations. When we reviewed CRA evaluations, we focused on retail banking services because they are the services evaluated as part of the CRA examination procedures.

[33]Our representative random sample of 219 CRA performance evaluations included examinations conducted in 2015 using large, intermediate small, and small institution examination procedures as the stratification factor on which we drew the independent random sample. In 2015, a small institution was defined as having less than $1.221 billion in assets, an intermediate small institution (a subset of small institutions) had at least $305 million but less than $1.221 billion in assets, and a large institution had $1.221 billion or more in assets. For more details on our sampling methodology, see appendix I.

Focus of CRA Examinations Varies by Institution Size and Business Model

The extent to which a financial institution's CRA examination includes an evaluation of retail banking services, small-dollar, nonmortgage consumer loans, and support for community development varies by the institution's size and business model. For example, consumer lending is generally not examined at large institutions unless it constitutes a substantial majority of a financial institution's lending.[34] Additional information about how these services and loans are evaluated for large, intermediate small, and small institutions follows.

Retail Banking Services

The CRA Q&As state that a CRA examination is to include an evaluation of the financial institution's provision of retail banking services in LMI areas for large institutions and may include such an evaluation for intermediate small institutions.[35] An evaluation of services is not required for small institutions. However, small institutions may request that their CRA examination include an evaluation of their services to possibly enhance their overall rating from "Satisfactory" to "Outstanding."[36] See figure 4 for a summary of which CRA examination types are to include evaluations of retail banking services and the factors considered.

[34]For small and intermediate small institutions, consumer loans may be chosen for review if these loans are a major product line for the institution.

[35]Along with the CRA examination procedures, the federal banking regulators periodically issue interagency Q&As to provide guidance to financial institutions and the public on the interpretation and application of the CRA regulations. The interagency Q&As give examples of retail banking services that improve access to financial services, or decrease costs, for LMI individuals, including low-cost deposit accounts, individual development accounts, and free or low-cost government, payroll, or other check cashing services. See *Interagency Questions and Answers Regarding Community Reinvestment* § __.24(a) – 1, 81 Fed. Reg. 48506, 48542 (July 25, 2016).

[36]Including an evaluation of a financial institution's services cannot be used to enhance a rating lower than "Satisfactory."

Figure 4: Evaluation of Retail Banking Services by CRA Examination Type

	Service test[a]	Community development test[b]	Optional review[c]
Factors considered	Examiners evaluate retail banking services including: • Geographic distribution of branches in low-, moderate-, middle-, and upper-income areas • Branch hours of operation • Loan and deposit products offered • Branch openings and closings • Alternative delivery systems, such as automated teller machines (ATM)	Examiners evaluate the extent to which the financial institution provides community development services through branches and other facilities in low- and moderate-income (LMI) areas.	If an institution chooses, examiners review its performance in providing branches and other services and delivery systems that enhance credit availability in its assessment area(s). Performance with respect to services may be used to enhance an institution's overall rating of "Satisfactory." Factors considered include: • Number of branches and ATMs • Number of branches and ATMs in LMI geographies compared to other geographies • Type and level of services provided at branches and by ATMs and alternative delivery systems • Branch openings and closings
Examination type			
Small institution			✓
Intermediate small institution		✓	
Large institution	✓		

✓ This area is addressed during this examination type

Source: GAO analysis of Community Reinvestment Act examination procedures. | GAO-18-244

[a]The service test also covers community development services, as discussed below.

[b]Services provided through branches are just one of many factors considered under the community development test, as discussed below.

[c]The optional review also includes a review of the institution's qualified investments, which are investments and grants that generally serve LMI individuals and areas.

Small-Dollar, Nonmortgage Consumer Loans

Large, intermediate small, and small institutions are subject to the lending test, but this test does not typically evaluate small-dollar, nonmortgage consumer loans.[37] The CRA examination procedures do not include an evaluation of a financial institution's provision of consumer loans in LMI areas unless (1) consumer loans constitute a substantial majority of the financial institution's lending (large institutions) or are a major product line (intermediate small and small institutions); (2) for a large institution, small-dollar, nonmortgage consumer loans are an example of an innovative or flexible lending practice; or (3) the institution requests that its consumer loans be evaluated.[38] Further, even in cases where consumer loans are evaluated, small-dollar, nonmortgage consumer loans may not be included because the institution may not provide such loans.[39] According to officials with the federal banking regulators, financial institutions typically do not collect and maintain data on small-dollar, nonmortgage consumer loans because of the low volume of such loans. See figure 5 for a summary of which CRA examination types are to include evaluations of small-dollar, nonmortgage consumer loans.

[37]The CRA Q&As state that loan programs that provide small, unsecured consumer loans in a safe and sound manner (based on the borrower's ability to repay) and with reasonable terms are an example of a lending activity that is likely to be responsive in helping to meet the credit needs of communities and therefore can get consideration under the lending test. See *Interagency Questions and Answers Regarding Community Reinvestment* § __.22(a) – 1, 81 Fed. Reg. 48506, 48536 (July 25, 2016). However, the current CRA examination procedures have not been updated to reflect these 2016 changes. The federal banking regulators are updating the examination procedures for all examination types, but do not have a time frame for completing that process.

[38]The federal banking regulators interpret "substantial majority" to be so significant a portion of the institution's lending activity by number and dollar volume of loans that the lending test evaluation would not meaningfully reflect its lending performance if consumer loans were excluded. FRB, FDIC, and OCC evaluate the "innovativeness or flexibility" of an institution's lending practices by reviewing the overall variety and specific terms and conditions of the credit products considered. They also consider the extent to which innovative or flexible terms or products augment the success and effectiveness of the institution's loan programs that address the credit needs of LMI geographies or individuals.

[39]Consumer loans also include motor vehicle loans, credit card loans, and home equity loans.

Figure 5: Evaluation of Small-Dollar, Nonmortgage Consumer Loans by CRA Examination Type

	Under the lending test as an innovative or flexible lending practice	Under the lending test based on loan volume or emphasis	Optional review
Factors considered	Examiners can consider small-dollar, nonmortgage consumer loans as an example of an innovative or flexible lending practice that, when present, can enhance a financial institution's rating.	Examiners may evaluate these loans at large institutions if consumer lending comprises a substantial majority of the institution's business.[a] Examiners may evaluate these loans at small and intermediate small institutions if consumer loans constitute a major product line.	If an institution so chooses and has collected and maintained required data, examiners will evaluate small-dollar, nonmortgage consumer loans.
Examination type			
Small institution		✓	✓
Intermediate small institution		✓	✓
Large institution	✓	✓	✓

✓ This area is addressed during this examination type

Source: GAO analysis of Community Reinvestment Act examination procedures. | GAO-18-244

[a]The federal banking regulators interpret "substantial majority" to be so significant a portion of a large institution's lending activity by number and dollar volume of loans that the lending test evaluation would not meaningfully reflect its lending performance if consumer loans were excluded.

Support for Community Development

The CRA examination procedures require that a CRA examination include an evaluation of a financial institution's support for community development in LMI areas for large and intermediate small institutions but not for small institutions.[40] However, small institutions may request that their CRA examination include an evaluation of their support for community development to possibly enhance a Satisfactory CRA rating to Outstanding. See figure 6 for a summary of which CRA examination types are to include evaluations of support for community development.

[40]As defined under CRA regulations, community development encompasses activities such as affordable housing for LMI individuals, community services targeted to LMI individuals, or activities that revitalize or stabilize LMI geographies.

Figure 6: Evaluation of Support for Community Development by CRA Examination Type

	Lending test	Investment test	Service test[b]	Community development test[c]	Optional review
Factors considered	Examiners evaluate: • Number and amount of community development loans • Responsiveness to opportunities for community development lending	Examiners evaluate: • Number and dollar amount of qualified investments[a] • Innovativeness and complexity of qualified investments • Degree to which these qualified investments are not routinely provided by other private investors • Responsiveness of qualified investments to available opportunities	Examiners evaluate: • Extent to which the institution provides community development services • Innovativeness and responsiveness of community development services • Range and accessibility of community development services provided in low-, moderate-, middle-, and upper-income geographies	Examiners evaluate: • Number and amount of community development loans and qualified investments • Extent to which the institution provides community development services, including the provision and availability of services to low- and moderate-income individuals • Institution's responsiveness to opportunities for community development lending, qualified investments, and community development services	If an institution chooses, examiners will review its qualified investments to determine if they enhanced credit availability in its assessment area and the institution's record of making such investments. Performance with respect to qualified investments may be used to enhance an institution's overall rating of "Satisfactory."
Examination type					
Small institution					✓
Intermediate small institution				✓	
Large institution	✓	✓	✓		

✓ This area is addressed during this examination type

Source: GAO analysis of Community Reinvestment Act examination procedures. | GAO-18-244

[a]Qualified investments include investments and grants that generally serve LMI individuals and areas.

[b]The large institution service test also covers retail banking services, as discussed above.

[c]The intermediate small institution community development test may cover retail banking services, as discussed above.

Our Analysis Found the Scope of 2015 CRA Performance Evaluations Was Consistent with These Procedures

Our review of a representative random sample of 219 performance evaluations for CRA examinations conducted in 2015 found that the extent to which retail banking services, small-dollar, nonmortgage consumer lending, and support for community development in LMI areas were evaluated was consistent with the elements included in the examination procedures.[41] That is, the extent to which these three areas were evaluated varied according to the type of examination and the institutions' business models. The discussion below presents estimates of and additional details on the extent to which the 2015 CRA examinations evaluated these three areas.[42]

Retail Banking Services

Our review of 2015 CRA performance evaluations found that the extent to which retail banking services were evaluated varied by institution size and business model, which was consistent with examination procedures. For large institutions, the specific types of services evaluated included the following:

- On the basis of the CRA performance evaluations reviewed, we estimated that 100 percent of the CRA examinations of large institutions conducted in 2015 included evaluations of each of the following types of retail banking services: branch locations and distribution; branch openings and closings; services provided; and hours of operation. Examples of the types of retail banking services that were evaluated included institution branches that were reasonably accessible to geographies and individuals of different income levels in the assessment area; branches that were readily

[41]Using data collection instruments based on the CRA examination procedures, we analyzed this sample of CRA performance evaluations to determine the extent to which they included evaluations of financial institutions' provision of retail banking services, small-dollar, nonmortgage consumer loans, and support for community development in LMI communities. Not every examination procedure followed during the CRA evaluation was included in the performance evaluations. CRA performance evaluations typically include a description of the financial institution; an overview of the scope of the examination; conclusions with respect to any performance tests; and the institution's rating. Additional information about any analysis or evaluations conducted as part of the review is included in supporting workpapers that are not publicly available. Our review of the workpapers for a sample of nine performance evaluations yielded no additional substantive information on retail banking services, small-dollar, nonmortgage consumer loans, or support for community development beyond what was included in the performance evaluations.

[42]The margin of error for all population estimates presented in each examination category (large, intermediate small, and small) is less than +/-11 percent at a 95 percent confidence level unless otherwise specified.

accessible to residents of low-income census tracts; and branch closures that had not adversely affected LMI communities.

- In terms of products offered, we estimated that 46 percent of the large institutions examined for CRA compliance in 2015 offered products that received consideration under the service test. FDIC officials told us that products are always evaluated under this test, but they may not receive CRA consideration and therefore would not be included in the performance evaluation.[43] FRB and OCC officials noted that products are always considered but may not be specifically mentioned in the performance evaluation. Examples of the types of products that were evaluated in the CRA examination included a variety of consumer banking products designed to help the unbanked, such as special checking accounts for individuals whose accounts had been closed and charged off by either the bank or another institution due to excessive overdrafts. In this example, the special account would be converted to a regular checking account after 1 year, and the financial institution would notify ChexSystems about the new account.[44] In another example, a bank offered a secured credit card designed to establish or rebuild credit histories.
- In terms of alternative delivery systems, we estimated that 97 percent of the examinations of large institutions conducted in 2015 evaluated the availability and effectiveness of such systems. Examples of alternative delivery systems that were evaluated included Internet banking, telephone banking, electronic bill pay, and mobile and text banking.

[43]As noted previously, not every examination procedure used during the CRA evaluation is included in the public report.

[44]ChexSystems is a check verification service and consumer credit reporting agency owned by the eFunds subsidiary of Fidelity National Information Services. Among other things, ChexSystems compiles information from banks and credit unions on accounts that have been closed due to account misconduct such as overdrafts, insufficient funds activity, returned checks, bank fraud, and check forgery. Banks and credit unions frequently assess applicants for new checking and other deposit accounts using products offered by resellers such as ChexSystems. In June 2006, we reported that banks we spoke with said that the name and identifying information of a customer seeking to open a new deposit account was typically run through the ChexSystems database. The reports provided back to the financial institution by ChexSystems typically included identifying information, as well as information useful in assessing an applicant’s risk, such as the applicant’s history of check orders and the source and details of any account misconduct. See GAO, *Personal Information: Key Federal Privacy Laws Do Not Require Information Resellers to Safeguard All Sensitive Data,* GAO-06-674 (Washington, D.C.: June 26, 2006).

Our review of CRA performance evaluations for intermediate small institutions found that retail banking services were generally evaluated, which was consistent with examination procedures. On the basis of the CRA performance evaluations reviewed, we estimated that 66 percent of the examinations of intermediate small institutions conducted in 2015 included an evaluation of services provided through branches and other facilities in LMI areas as part of the community development test. Officials at the three federal banking regulators told us that the community development test considers multiple factors, and services provided through branches are not always evaluated. Examples of services that were evaluated included delivery systems that were reasonably accessible to individuals of different income levels; extended branch operating hours available at all drive-up locations on Fridays; and the availability of all of an institution's loan and deposit products at all locations.

Our review of CRA performance evaluations for small institutions found that retail banking services were evaluated in a small percentage of the reports, which is consistent with such an evaluation not being required but being made only at the request of the institution. On the basis of the CRA performance evaluations reviewed, we estimated that 6 percent of the examinations of small institutions conducted in 2015 included an evaluation of investments and retail banking services.[45] One of the small institutions evaluated provided a variety of deposit accounts—including accounts with low opening balance requirements, unlimited check writing privileges, no monthly fees, and free access to electronic banking services—that could accommodate lower-income individuals and other customers to help them maintain banking relationships with a federally-insured financial institution.

Small-Dollar, Nonmortgage Consumer Loans

Our review of 2015 CRA performance evaluations found that small-dollar, nonmortgage consumer loans were evaluated in a small percentage of the reports reviewed—which was consistent with examination procedures. As discussed previously, consumer loans are not evaluated as part of a CRA examination unless (1) consumer loans constitute a substantial majority of a large financial institution's lending or are a major

[45]In our sample of small institution CRA performance evaluations, five institutions requested a review of their retail banking services in order to possibly enhance their overall rating from Satisfactory to Outstanding. However, only one of these five institutions received an Outstanding rating. The reports did not indicate why there was no improvement in the overall rating for the other four institutions.

product line chosen for review at small or intermediate small institutions, (2) for a large institution, small-dollar, nonmortgage consumer loans are an example of an innovative or flexible lending practice, or (3) the institution requests that consumer loans be evaluated. Further, even in cases where consumer loans are evaluated, small-dollar, nonmortgage consumer loans may not be included because the institution may not provide such loans.

- **Large institutions.** On the basis of the CRA performance evaluations we reviewed, we estimated that 25 percent of the examinations of large institutions conducted in 2015 included an evaluation of small-dollar, nonmortgage consumer loans as an innovative or flexible product. An example of a loan type that was evaluated included a consumer loan product with a maximum 36 percent APR and a term that ranged from 6 months to 1 year. The CRA report noted that this loan offering was responsive to a need identified by community groups.
- **Intermediate small institutions.** On the basis of CRA performance evaluations we reviewed, we estimated that 3 percent of the examinations of intermediate small institutions conducted in 2015 included an evaluation of small-dollar, nonmortgage consumer loans. An example of a loan type that was evaluated was very small loans to individuals with limited resources. The related report noted the institution had 166 active small-dollar, nonmortgage consumer loans with an originating balance of less than $1,000, and 303 active loans with an originating balance of between $1,000 and $1,500. (The smallest originating loan amount was $200.)
- **Small institutions.** On the basis of CRA performance evaluations we reviewed, we estimated that 6 percent of the examinations of small institutions conducted in 2015 included an evaluation of small-dollar, nonmortgage consumer loans. An example of a loan type that was evaluated was a small-dollar loan program offered as an alternative to payday loans, for amounts up to and including $2,500. The related report noted that the institution had originated 109 such loans ranging in size from $153 to $2,500 for a total dollar volume of $158,610.

Support for Community Development

Our review of 2015 CRA performance evaluations found that support for community development was evaluated for all large and intermediate small institutions and for a very small percentage of small institutions, which was consistent with examination procedures. As discussed previously, a CRA examination is to include an evaluation of a financial institution's support for community development in LMI areas for large

institutions and intermediate small institutions. An evaluation of support for community development is not required for small institutions, but they may request such an evaluation of support for community development to possibly enhance a Satisfactory CRA rating to Outstanding.

On the basis of CRA performance evaluations we reviewed, we estimated that 100 percent of the examinations of large institutions conducted in 2015 included an evaluation of community development lending, qualified investments, and community development services provided. An example of the types of support for community development that were evaluated included an institution originating four community development loans in the amount of $1.5 million in its assessment areas. In the related report, it was noted that this was an improvement from the institution's prior examination in which the institution had not originated any community development loans.

Our review of 2015 CRA performance evaluations for intermediate small institutions also found that support for community development was evaluated.

- On the basis of the CRA performance evaluations we reviewed, we estimated that 100 percent of the examinations of intermediate small institutions conducted in 2015 included an evaluation of qualified investments and community development services as part of the community development test. Examples of these types of support for community development that were evaluated included (1) the financial institution making 39 donations totaling $27,471 and (2) the financial institution's representatives leading efforts to provide financial, technical, or leadership advice for several organizations that foster economic development, affordable housing, or social services to LMI individuals.
- In addition, we estimated that 99 percent of these intermediate small institution examinations included an evaluation of community development lending as part of the community development test. For example, one report noted that the institution's community development loans were responsive to community development needs, especially in the areas of economic development, affordable housing, and revitalization and stabilization of LMI areas.

Our review of CRA performance evaluations for small institutions found that support for community development was evaluated in a small percentage of reports, which is consistent with such an evaluation being made only at the request of the institution. On the basis of CRA

performance evaluations we reviewed, we estimated that 6 percent of the examinations of small institutions conducted in 2015 included an evaluation of community development investments.[46] An example of a community development investment that was evaluated was a small financial institution's creation of a community development corporation to help address the housing shortage for LMI individuals in the community.[47]

As discussed later in this report, some stakeholders commented that examiners may not consistently implement the CRA examination procedures. We found during our review of 2015 CRA performance evaluations that it was not possible to determine whether there were any inconsistencies in the application of procedures by CRA examiners. The performance evaluations we reviewed did not contain sufficient details on specific services or loans to determine whether they were evaluated the same way at different institutions.[48] In addition, FRB, FDIC, and OCC officials pointed out the need for CRA examiners to use their professional judgment in arriving at conclusions about financial institution performance, particularly as it pertains to performance context. Performance context is a broad range of economic, demographic, and institution- and community-specific information that an examiner reviews to understand the context in which a financial institution's record of performance should be evaluated. CRA examiners will review the demographics and credit needs of the financial institution's assessment area, the financial institution's business strategy, and competition within the assessment area in forming the performance context.

The three federal banking regulators take a number of steps to help ensure consistency. As previously discussed, CRA examiners use a

---

[46]In our sample of small institution CRA performance evaluations, five institutions requested a review of their community development investments in order to possibly enhance their overall rating from Satisfactory to Outstanding. However, only one of these five institutions received an Outstanding rating. The reports did not indicate why there was no improvement in the overall rating for the other four institutions.

[47]Community development corporations are not-for-profit organizations incorporated to provide programs, offer services, and engage in other activities that promote and support community development. They usually serve a geographic location such as a neighborhood or a town. They often focus on serving lower-income residents or struggling neighborhoods. They can be involved in a variety of activities such as economic development, education, community organizing, real estate development, and affordable housing.

[48]Due to confidentiality concerns, details about services and loans can only be found in the examiners' workpapers.

common set of interagency examination procedures to better ensure consistency. Further, agency officials told us that CRA examiners receive training on all of the CRA examination procedures. Our review of CRA examiner training materials showed that provision of retail banking services; small-dollar, nonmortgage consumer loans; and support for community development was covered. Officials with the three agencies also noted that each CRA examination report undergoes supervisory review to ensure that examiners followed examination procedures and guidelines. For example, FRB officials told us that while the CRA examination processes and procedures are the same at every Federal Reserve Bank, not every examiner will conduct CRA examinations exactly the same way. They stated that FRB's Reserve Bank Oversight section reviews CRA performance evaluations and conducts operational reviews to minimize such differences. When variations are noted and pointed out to examiners, the officials stated it results in more consistency over time. Further, the officials noted that FRB's Division of Consumer and Community Affairs recently completed a systematic review of CRA examinations. As a result of that review, FRB issued feedback reports to each of the Federal Reserve Banks in May 2017.[49] Similarly, both FDIC and OCC officials told us that they have a separate quality assurance function to ensure CRA examiners followed examination procedures and guidelines.

[49]The contents of the feedback reports were for the use of the individual Federal Reserve banks only and were not publicly available.

Suggested Options Reflect Need to Balance Serving LMI Consumers with Concerns about Profitability and Safety and Soundness

Many stakeholders suggested options for implementing CRA that could encourage financial institutions to provide more basic banking services and small-dollar, nonmortgage consumer loans to LMI individuals, but they noted trade-offs.[50] However, some stakeholders noted that some options may not be economically feasible and therefore institutions' concerns about profitability and safety and soundness may outweigh any perceived benefits of CRA ratings. Accordingly, stakeholders suggested options outside of CRA implementation such as loosening underwriting restrictions on loans under a certain dollar amount and clarifying what percentage rate on loans is considered allowable by regulators to further encourage institutions to make more of these loans.

Options to Change CRA to Help Encourage Basic Banking Services and Small-Dollar Loans Would Involve Trade-offs

According to knowledgeable stakeholders, options that would change how CRA is implemented could further encourage financial institutions to provide basic banking services and small-dollar, nonmortgage consumer loans in LMI areas. Such options could include modifications to tests conducted as part of the CRA examination process, expanding the areas and entities assessed as part of the examinations, and clarifying guidance about the examination process. However, each would involve trade-offs.

Revising the CRA Service Test to Give More Consideration to Basic Banking Services

In the literature we reviewed and interviews, stakeholders suggested ways that the CRA service test could be improved to further encourage financial institutions to provide basic banking services in LMI areas. Suggested modifications to the service test include:

- **Applying the service test to small financial institutions.** The service test is required only for large financial institutions, but small institutions may request that aspects of their services be evaluated. For example, small institutions may request that their performance in making qualified investments and in providing branches and other services and delivery systems that enhance credit availability in their

[50]Stakeholders included representatives of think tanks, academia, advocacy groups, financial institutions or industry associations, federal banking regulators, and other government agencies. We identified suggested options by conducting stakeholder interviews and reviewing literature. To obtain information on the relative importance of these suggested options, we sent a survey to 66 stakeholders (individuals and organizations). We then obtained stakeholder views on options identified in the survey as the most important by holding a series of discussion groups. For more information about our methodology for identifying suggested options and obtaining stakeholder views on these options, see appendix I.

assessment area(s) be considered.[51] Several stakeholders suggested that the service test should be mandatory for small institutions so that the services they provide—including the distribution of available branches in LMI areas—are assessed. For example, one study that suggested this stated that there was ample evidence that the need for basic financial services was poorly served by banks, citing the decline and relative under-representation of bank branches in low-income and minority neighborhoods.[52] It also noted that high-cost retail financial services, such as payday lenders, had emerged. The study concluded that the service test offered only a weak incentive to reverse this trend, in part because most banks are not subject to it and therefore the number and location of branches they provide are not assessed.

Officials with the three federal banking regulators indicated it was not necessary to revise the CRA service test to make it applicable to financial institutions of all sizes. Specifically, they noted that if a small institution is particularly good at offering targeted services, it has the option of requesting that these services be evaluated. However, FDIC officials acknowledged that few small institutions elect to do so. Further, officials noted that the community development test—which applies to intermediate small institutions—encourages them to provide services. As noted previously, the examination procedures state that intermediate small institutions are evaluated under the community development test on the extent to which they provide community development services. This can include services provided through branches. However, our review of a representative sample of 2015 CRA performance evaluations found that not all intermediate small financial institutions were evaluated on services provided through their branches. Additionally, one federal banking regulator representative noted that small institutions, particularly community banks, already are dissatisfied with the high number of regulations they are subject to.

- **Evaluating the usage and effectiveness of products and services.** Several stakeholders suggested that the service test should evaluate not just what products financial institutions offered for LMI consumers but also how effective the products were and how often they were used by consumers. For example, one paper suggested strengthening

[51]Small institutions may request to be evaluated in these areas to try to improve a Satisfactory rating to an Outstanding rating.

[52]R. Quercia, J. Ratcliffe, and M. Stegman, “The Community Reinvestment Act: Outstanding, and Needs to Improve,” in *Revisiting the CRA: Perspectives on the Future of the Community Reinvestment Act* (Boston and San Francisco: A Joint Publication of the Federal Reserve Banks of Boston and San Francisco, 2009), 47-58.

the service test by, among other things, consistently analyzing the size of low-cost account programs, basing examinations of large institutions on the number of accounts per census tract, and evaluating alternative delivery systems based on effectiveness.[53] Alternative delivery systems allow consumers to access financial institutions using nontraditional methods such as ATMs, Internet banking, and mobile banking. The paper explained that alternative systems should be evaluated based on actual usage rates that measure effectiveness and extent of service, and not be credited simply because they are in place. It noted that creating a more objective scorecard for measuring performance under the CRA service test could increase banks' responsiveness to the needs of the underbanked. Similarly, another study suggested evaluating the number of LMI account holders an institution has and whether they hold traditional or more innovative accounts.[54] It concluded that quantitative measures should allow an institution's performance to be better portrayed under the service test. Representatives from an advocacy group we interviewed stated that the service test should be more rigorous because when examiners cite innovative banking services, they usually do not provide data on the number and volume of these services or describe why they are considered innovative or low cost.

Multiple participants in our advocacy discussion group also suggested collecting additional data under the service test would allow for a more quantifiable way to assess a financial institution's performance. However, one participant explained that revising the service test to require additional data on deposit accounts would not be received well by the industry as banks would be likely to object to the cost associated with collecting new data.

FDIC officials told us that the CRA Q&As address the usage and effectiveness of products and services.[55] However, they noted they

[53]M. Stegman, K. Cochran, and R. Faris, "Creating a Scorecard for the CRA Service Test," Brookings Policy Brief, no. 96 (March 2002).

[54]M. Barr, "Community Reinvestment Emerging from the Housing Crisis," in *Revisiting the CRA: Perspectives on the Future of the Community Reinvestment Act* (Boston and San Francisco: A Joint Publication of the Federal Reserve Banks of Boston and San Francisco, 2009), 170-177. OCC officials commented that income data are not currently available for deposit holders and "traditional" and "innovative" accounts would have to be defined.

[55]FDIC officials noted that the following CRA Q&As address usage and effectiveness: § __.21(a)-3; .24(a)-1; .24(d)-1; .24(d)(3)-1 and .28(b)-1. 81 Fed. Reg. 48506 (July 25, 2016).

could not speak to potential gaps in examiners actually following this guidance. Further, participants in our federal banking regulator discussion group noted that regulators expanded consideration of usage of banking services in updated CRA Q&As published in July 2016.[56] The updated Q&As state that one of six factors that examiners may consider to determine whether a financial institution's alternative delivery system is an available and effective means of delivering retail banking services in LMI geographies and to LMI individuals is the rate of adoption and use.[57] However, financial institutions are not required to provide such information and this provision only applies to alternative delivery systems.

- **Penalizing activities that undermine the provision of quality services.** Several stakeholders suggested that CRA examiners could reduce the scores they give financial institutions on the service test for engaging in activities that do not protect LMI consumers. For example, one study stated that CRA examiners should reduce the scores they give institutions that are in arrangements with affiliates or other parties that do not provide adequate consumer protection.[58] Another study suggested a similar change because CRA does not discourage counter-productive behaviors such as offering free checking accounts with costly overdraft protection.[59]

  Two participants in our advocacy discussion group supported giving lower CRA scores to financial institutions that received large revenues from overdraft fees, with one noting that it would be difficult to get banks to offer reasonably priced small-dollar loans as long as overdraft programs remain so lucrative. However, participants in our think tank and industry discussion groups were concerned that revising the service test to penalize bank activities that undermine the provision of quality services could change CRA into a compliance exam, rather than a means of encouraging financial institutions to

---

[56]The federal banking regulators issued updates to the CRA Q&As in July 2016 after accepting and considering public comments on proposed updates. 81 Fed. Reg. 48506 (July 25, 2016).

[57]*Interagency Questions and Answers Regarding Community Reinvestment* § __.24(d)(3) – 1. 81 Fed. Reg. 48506, 48542 (July 25, 2016). The other five factors are: ease of access (physical or virtual), cost to consumers as compared with the institution's other delivery systems, the range of services delivered, the ease of use, and the reliability of the system.

[58]M. Barr, "Community Reinvestment Emerging from the Housing Crisis," 170-177.

[59]R. Quercia, J. Ratcliffe, and M. Stegman, "The Community Reinvestment Act: Outstanding, and Needs to Improve," 47-58.

provide such services. Similarly, one participant in the industry group noted that a bank's overdraft revenue was not relevant to encouraging small-dollar lending to LMI communities and therefore should not be included in the CRA process.

Consistent with the concerns expressed by these stakeholders, one participant in the industry discussion group noted that expanding the service test to explicitly examine the amount of overdraft fees collected by financial institutions is unnecessary. An official who was part of our federal banking regulator discussion group noted that unfair and deceptive acts and practices—which could include excessive overdraft fees—are already evaluated under the consumer compliance examinations that the federal banking regulators also conduct. Such consumer compliance examinations assess financial institutions' compliance with federal consumer protection laws and fair lending statutes and regulations. The examination procedures for CRA examinations call for the regulators to review the results of the most recent compliance examination and determine whether evidence of discriminatory or other illegal credit practices should lower the institution's CRA rating.

- **Rewarding financial institutions for additional products and services, such as helping LMI consumers build wealth through savings accounts.** Stakeholders suggested several additional products and services that they thought should get consideration under the service test. For example, one former FDIC chair we spoke with stated that regulators should give financial institutions credit for helping consumers build wealth through savings accounts. A group that commented on the proposed updates to the CRA Q&As suggested providing CRA credit to those institutions offering clearing and processing services to other institutions that (1) provide fair and low-cost remittance services below market average prices to underserved communities, (2) offer entry-level banking services for the unbanked that can help provide access to additional financial services in those underserved communities, and (3) serve companies or institutions that have had difficulty securing clearing and processing

services.[60] A survey respondent suggested that consideration be given under the service test for digital banking services with a specific link to underserved and LMI markets. That respondent recommended credit under the service test for offering second-chance checking accounts to customers with a prior negative account history.

Two regulatory stakeholders were cautious about suggested options in this area. For example, a participant in our nonfederal banking regulator discussion group explained that brick-and-mortar bank locations are important to LMI communities and the service test should not be modified in such a way that institutions would not get credit for those brick-and-mortar locations. Additionally, a participant in our federal banking regulator discussion group mentioned that the CRA Q&As make reference to low-cost accounts and other services that banks can provide to get CRA consideration.[61] However, these banking services are currently evaluated for large institutions only.

Revising the CRA Lending Test to Give More Consideration for Small-Dollar, Nonmortgage Consumer Loans

Stakeholders suggested evaluating the quality of loans and providing more consideration under the lending test for small-dollar, nonmortgage consumer loans. One advocacy group representative told us that because small-dollar loans are not profitable, revising the lending test would give banks a regulatory incentive to make such loans. However, an industry representative noted that due to the economics and risks of small-dollar loans, banks would need to receive considerable consideration for them under the lending test for this incentive to work. Industry representatives further noted that if the economics of such loans do not work, CRA will have little effect regardless of any changes to the lending test. Stakeholders suggested the following three modifications to the lending test:

---

[60]Check clearing or bank clearance is the process of moving a check from the bank in which it was deposited to the bank on which it was drawn, and the movement of the money in the opposite direction. This process is called the clearing cycle and normally results in a credit to the account at the bank of deposit, and an equivalent debit to the account at the bank on which it was drawn. Remittance services include many types of international transfers including cash-to-cash money transfers, international wire transfers, some prepaid card transfers, and automated clearing house transactions. The automated clearing house is a system that clears and settles batched electronic transfers for participating depository institutions.

[61]In *Interagency Questions and Answers Regarding Community Reinvestment* § __.24(a) – 1, the regulators state that the following are examples of retail banking services that improve access to financial services, or decrease costs, for LMI individuals: low-cost deposit accounts; free or low-cost government, payroll, or other check cashing services; and reasonably priced international remittance services. 81 Fed. Reg. 48506, 48542 (July 25, 2016).

- **Evaluating quality of loans.** Stakeholders suggested more focus on loan quality. An advocacy group representative we interviewed suggested CRA examiners could use the proposed CFPB regulations on acceptable consumer credit to assess small-dollar, nonmortgage consumer loans.[62] One study noted that many banks provide the funding to support payday lenders, lenders that may charge APRs of nearly 400 percent on short-term loans.[63] The authors stated that funding such lending undermines financial security, and banks should receive negative (and certainly not positive) scores on their CRA tests for doing so.

  One participant in the industry discussion group expressed concern about revising the lending test in a way that would penalize financial institutions for the underwriting methods they used to originate small-dollar consumer loans. The participant explained that having more scrutiny of such loans could cause small-dollar loans to become too costly to make. A non-CRA regulatory discussion group participant mentioned that institutions are already subject to consumer compliance examinations, which assess compliance with federal consumer protection laws.

  Consistent with participants in the industry discussion group, the federal banking regulators indicated that examiners consider any information related to discriminatory or illegal credit practices found during compliance examinations when a final CRA rating is assigned. FDIC officials also noted that the CRA Q&As call for qualitative factors to be considered under the lending test.[64]

- **Collecting more data on consumer lending.** There are no CRA data reporting requirements for consumer loans. Representatives from an advocacy organization suggested that the federal banking regulators collect such data for banks with sizable amounts of this type of lending. They noted that such data could then be aggregated into a database that would give some indication of the extent to which consumer lending is reaching LMI borrowers. Additionally, a participant in our advocacy discussion group noted that financial institutions might appreciate a more systematic collection of data on

[62]As discussed later in this report, the CFPB regulations were finalized on November 17, 2017.

[63]R. Quercia, J. Ratcliffe, and M. Stegman, “The Community Reinvestment Act: Outstanding, and Needs to Improve,” 47-58.

[64]FDIC officials cited § __.21(a)-3; .22(a)-1; and .28(b)-1. 81 Fed. Reg. 48506 (July 25, 2016).

consumer lending that would enable them to compare themselves to their peers in the marketplace. However, collecting and maintaining additional data would present a cost to financial institutions. One advocacy group representative stated that there is a need to balance the benefits of additional data collection with the burden of collecting these data. Officials with the federal banking regulators did not comment on this suggested change.

- **Providing more credit under the lending test for small-dollar, nonmortgage consumer loans.** Some stakeholders suggested giving financial institutions additional CRA credit for small-dollar, nonmortgage consumer loans. First, in comments on the proposed changes to the CRA Q&As, a nonprofit organization stated that the lending test should be revised to provide more incentives for CRA-regulated institutions to enter geographies where there is a high penetration of high-cost lenders. Second, an advocacy group representative suggested that more CRA credit go to providing low-cost consumer loans using innovative products. Third, FDIC reported that participants in its small-dollar loan pilot program suggested small-dollar lending should receive more emphasis in CRA examinations, even if the particular program is small.[65]

  One participant in our advocacy discussion group explained that small-dollar loans are not profitable, so revising the lending test would give banks a regulatory incentive to make such loans. A participant in our industry discussion group suggested giving specific credit for providing small-dollar loans in low-income areas, even if they do not comprise a substantial majority of a financial institution's lending. However, two other participants stated that due to the economics and risks of small-dollar loans, banks would require a lot of CRA credit for this incentive to counteract those concerns. Further, participants in our think tank discussion group expressed a concern that increasing the importance of small-dollar loans would dilute the CRA's emphasis on home mortgage lending.[66]

In commenting on these suggested modifications to the lending test, officials with the federal banking regulators told us CRA examiners

[65]Federal Deposit Insurance Corporation, "A Template for Success: The FDIC's Small-Dollar Loan Pilot Program," *FDIC Quarterly*, vol. 4, no. 2 (2010).

[66]CRA was enacted, in part, in response to concerns about redlining, or banks' refusal to offer home loans in certain neighborhoods based on the income or racial composition of the area. Because home mortgages are a primary lending product for many banks, they are often a key component of CRA reviews.

determine how much consideration to give for small-dollar, nonmortgage loans based on the responsiveness of such lending to community needs and performance context. They noted that an institution's performance context includes elements such as institutional capacity and constraints and lending opportunities in the financial institution's assessment area. However, as the lending test relies heavily on an evaluation of the institution's loan products that comprise a substantial majority of its lending or are a major product line, small-dollar loans would rarely be considered.

Expanding CRA Assessment Areas to Include Services or Loans Provided Outside of a Financial Institution's Geographic Area

In the literature we reviewed and interviews, stakeholders suggested that regulators could broaden the definition of a bank's assessment area to better reflect financial markets as they exist today rather than as they were when CRA was enacted in 1977. This would allow examiners to get a better understanding of how well an institution is serving LMI communities, because the geographic area subject to examination would be broader. For example, one article explained that when CRA was enacted banks received deposits and made loans through branches, but today there are banks that make the majority of their loans through brokers and other non-branch means.[67] Another article noted that given the dramatic changes in the financial landscape, including new organizational structures (such as financial holding companies, multinational financial enterprises, and nonbank lenders) and new delivery mechanisms (such as Internet, mobile, and phone banking), the traditional concept of the assessment area no longer captures a lender's community.[68] A third article noted that consolidation, regulatory change, expansion, and technology have loosened the geographic constraints once faced by traditional branch banking.[69]

Stakeholders were mixed in their views on the extent to which expanding assessment areas would further encourage financial institutions to

[67]J. Taylor and J. Silver, "The Community Reinvestment Act: 30 Years of Wealth Building and What We Must Do to Finish the Job," in Revisiting the CRA: Perspectives on the Future of the Community Reinvestment Act (Boston and San Francisco: A Joint Publication of the Federal Reserve Banks of Boston and San Francisco, 2009), 148-159.

[68]R. Essene and W. Apgar, "The 30th Anniversary of the CRA: Restructuring the CRA to Address the Mortgage Finance Revolution," in *Revisiting the CRA: Perspectives on the Future of the Community Reinvestment Act* (Boston and San Francisco: A Joint Publication of the Federal Reserve Banks of Boston and San Francisco, 2009), 12-29.

[69]R. Quercia, J. Ratcliffe, and M. Stegman, "The Community Reinvestment Act: Outstanding, and Needs to Improve," 47-58.

provide basic banking services and small-dollar, nonmortgage consumer loans. A participant in our advocacy discussion group stated that if banks are providing basic banking services and small-dollar loans outside current assessment areas, expansion of the definition would be helpful. However, a participant in the same group noted that there is little data on where banks deliver such services and products, so it may be difficult to determine whether an expansion of the definition of a bank's assessment area is needed. A participant in our think tank discussion group also noted that expanding assessment areas was unlikely to boost small-dollar loan offerings because small-dollar loans tend to be unprofitable. Federal banking regulator officials explained that it would be difficult to come up with a singular definition for assessment areas that applies across a variety of different business models. However, as others have pointed out, the current definition does not always align with modern practices.

Other stakeholders were concerned about the effect that expanding assessment areas to include electronic transactions might have on physical branch locations. One advocacy group representative noted that technological solutions that enable banks to service customers outside of their physical locations are not a substitute for bank branch and deposit services. In the updated CRA Q&As issued in July 2016, the federal banking regulators agreed, explaining that they were withdrawing some proposed revisions to avoid the unintended inference that branches are less important in providing financial services to LMI geographies.[70]

The federal banking regulators noted examiners can already consider activities outside of a financial institution's assessment areas. Specifically, the CRA Q&As state that examiners may consider loans, including loans to LMI borrowers, outside a financial institution's assessment areas,

[70]The regulators proposed to revise *Interagency Questions and Answers Regarding Community Reinvestment* § __.24(d) – 1, which addresses how examiners should evaluate the availability and effectiveness of an institution's systems for delivering retail banking services. Specifically, they proposed to delete the statements that "performance standards place primary emphasis on full-service branches" and that alternative delivery systems are considered "only to the extent" that they are effective alternatives in providing needed services to low- or moderate-income geographies and individuals. The proposal was intended to encourage broader availability of alternative delivery systems to low- or moderate-income geographies and individuals without diminishing the value full-service branches offer to communities. Almost all community organization commenters opposed the proposed revisions, asserting that branches continue to be uniquely important to low- and moderate-income neighborhoods. 81 Fed. Reg. 48506, 48515 (July 25, 2016).

provided the institution has adequately addressed the needs of borrowers within its assessment area.[71]

Expanding CRA to Include All Affiliates of Financial Institutions and Additional Entities Such as Credit Unions and Nonbanks

Stakeholders suggested changing regulations to require inclusion of bank affiliates in CRA examinations and revising the CRA statute to expand CRA to entities outside of banks.[72] Specifically, stakeholders suggested the following two modifications:

- **Revising regulations to require inclusion of financial institution affiliates and subsidiaries in CRA examinations.** A number of articles we reviewed outlined concerns with allowing financial institutions to choose whether to include their affiliates in their CRA examinations. One article stated that banks may choose to include their affiliates in their CRA examinations if the affiliates' activities will be viewed positively by examiners but exclude them otherwise.[73] Another article noted that illegal practices on the part of a bank's affiliate would count against the institution only if the bank elects to have its affiliate's lending activity included in the examination.[74] Another article suggested that any for-profit subsidiary or holding company affiliate that provides any essential products be evaluated in the same manner and at the same time as the largest bank or thrift in the holding company group.[75]

  One participant in our advocacy discussion group noted that mandatory inclusion of affiliates in CRA examinations would allow for downgrades to automatically apply if the affiliate is originating loans that are harmful to LMI consumers. A second participant in the same group stated including affiliates in CRA assessments could discourage banks from sending LMI clients who do not qualify for their loans to affiliates for subprime loans. The first participant agreed and

[71]See *Interagency Questions and Answers Regarding Community Reinvestment* §__.22(b)(2) & (3)—4.

[72]Under current regulations, financial institutions are allowed to choose whether their affiliates are included in their CRA examinations.

[73]J. Taylor and J. Silver, "The Community Reinvestment Act: 30 Years of Wealth Building and What We Must Do to Finish the Job," 148-159.

[74]See R, Quercia, J. Ratcliffe, and M. Stegman, "The Community Reinvestment Act: Outstanding, and Needs to Improve," 47-58.

[75]E. Seidman, "A More Modern CRA for Consumers," in *Revisiting the CRA: Perspectives on the Future of the Community Reinvestment Act* (Boston and San Francisco: A Joint Publication of the Federal Reserve Banks of Boston and San Francisco, 2009), 105-114.

noted that expanding CRA to include affiliates could discourage banks from investing in abusive payday lenders. Similarly, a participant in our industry discussion group stated that expanding CRA to cover finance companies that were owned by a bank or that a bank had some financial interest in could help combat predatory lending.

In their 1995 revisions to the CRA regulations, FRB, FDIC, and OCC noted that many industry commenters opposed consideration of affiliate lending except at the institution's option on the ground that consideration without the institution's consent may be equivalent to extending CRA coverage to affiliates that may not be subject to the statute.[76] Some community and consumer groups supported consideration of affiliate activity and urged that the regulatory language be strengthened to require the agencies to take affiliate lending into account under certain circumstances. In the final rule, affiliate lending is considered only at the election of the institution, except with regard to the lending activity criterion, where it will provide context for the assessment in order to discourage an institution from inappropriately influencing an evaluation of its CRA performance by conducting activities that would be viewed unfavorably in an affiliate.

- **Revising the CRA statute to expand CRA to nonbanks.** Stakeholders also suggested expanding CRA to nonbanks such as credit unions, investment banks or broker dealers, and emerging nonbank lenders. First, an issue brief from an advocacy group suggested that applying CRA to mainstream credit unions would bolster their branching and lending to LMI populations, noting that credit unions were more apt to retreat from modest-income neighborhoods during the Great Recession in part because banks have CRA obligations while credit unions do not.[77] Participants in our think tank discussion group also discussed bringing credit unions under CRA-like regulations, agreeing that requirements to perform CRA-like duties in return for maintaining charters or a designation as a community development financial institution (CDFI) would make sense.[78] However, one participant in our nonfederal banking regulator discussion group stated it was not necessary to expand CRA to

[76]60 Fed. Reg. 22156 (May 4, 1995).

[77]National Community Reinvestment Coalition, "Why Branch Closures Are Bad for Communities" (Washington, D.C.: April 2012).

[78]CDFIs expand economic opportunity in low-income communities by providing access to financial products and services for local residents and businesses. They can be banks, credit unions, loan funds, microloan funds, or venture capital providers.

include credit unions because credit unions are owned by their members and therefore are already playing a vital role in their community.

Second, one study suggested including additional institutions, such as investment banks or broker-dealers, in return for access to the Federal Reserve's discount window.[79] The study explained that expanding CRA to the same institutions that benefited from that safety net would result in greater consumer access to the full range of financial services. Third, another study suggested that CRA should be uniformly expanded to cover newly emerging nonbank lenders, such as independent mortgage banking companies.[80] The study suggested that because nonbanks are not uniformly regulated, consumers cannot rely on the uniform benefits of legally mandated federal oversight.

However, one participant in our industry discussion group suggested that if CRA does not effectively incentivize banks to offer small-dollar loans to LMI consumers, then expanding it to additional entities may not address that issue. Another participant elaborated, stating that nonbanks, like banks, will only make small-dollar loans if such loans are profitable, regardless of whether they are subject to CRA. Further, the federal banking regulators stated that expanding CRA to include additional entities would probably capture more of the small business and home mortgage markets. However, they added that expanding CRA to include more entities would require legislative action because they lack the authority to do so.

Issuing Additional CRA Guidance

CRA guidance includes regulations, publicly available examination procedures, and Q&As. In the literature we reviewed and interviews, stakeholders suggested that additional specific information in this

[79]L. Cohen and R. Agresti, "Expanding the CRA to All Financial Institutions," in *Revisiting the CRA: Perspectives on the Future of the Community Reinvestment Act* (Boston and San Francisco: A Joint Publication of the Federal Reserve Banks of Boston and San Francisco, 2009), 134-137. When the Federal Reserve System was established in 1913, lending reserve funds through the discount window was intended as the principal instrument of central banking operations. Although the window was long ago superseded by open market operations as the most important tool of monetary policy, it still plays a complementary role. The discount window functions as a safety valve in relieving pressures in reserve markets; extensions of credit can help relieve liquidity strains in a depository institution and in the banking system as a whole. The window also helps ensure the basic stability of the payment system more generally by supplying liquidity during times of systemic stress.

[80]R. Essene and W. Apgar, "The 30th Anniversary of the CRA: Restructuring the CRA to Address the Mortgage Finance Revolution," 12-29.

guidance on basic banking services and small-dollar, nonmortgage consumer loans could further encourage financial institutions to provide such services and loans. For example, representatives from an advocacy organization suggested that the CRA Q&As be updated to provide more specific examples of basic banking services and small-dollar, nonmortgage consumer loans that can receive CRA credit.

Three participants in our think tank discussion group believed that issuing additional guidance was necessary because banks they previously spoke with indicated a lack of guidance and general uncertainty about acceptable products was preventing them from moving forward with new products. For example, one participant noted that greater certainty on what regulators consider to be acceptable products might make lenders more willing to invest the necessary resources to create new products. One participant in our nonfederal banking regulator discussion group agreed that more guidance and clarification on how different activities are viewed by CRA examiners would be the most useful way to communicate that these activities will receive CRA credit. Specifically, she stated that it is important to communicate through the Q&As or examiner training the goal of encouraging banks to make more small-dollar, nonmortgage loans. One example of such guidance would be preparing a template of an acceptable small-dollar loan product, such as the one resulting from FDIC's small-dollar loan pilot.

Participants in our advocacy and industry discussion groups further explained that clear guidance would help address variation in how different CRA examiners interpret CRA provisions. One participant in our industry discussion group also noted inconsistencies across examiners and commented that more guidance would be helpful in reducing such inconsistencies. In particular, the participant noted that examiners could benefit from additional guidance that clarifies that small-dollar loans will have higher losses because of the increased risk associated with these products. Other discussion group participants agreed but noted that issuing additional guidance may be problematic. One participant in our advocacy discussion group noted that the additional guidance federal banking regulators issue is generally limited to revisions to the interagency Q&As, which may not be seen as requirements. Additionally, a participant in our industry discussion group noted it may be difficult for regulators to agree on additional guidance in a timely manner. For example, the most recent revisions to the Q&As took two years to finalize.

Another participant in the industry discussion group indicated that guidance could evolve into actual requirements and thereby become

narrowly focused. Further, one participant in our nonfederal banking regulator discussion group stated that the federal banking regulators would need to ensure that additional guidance did not create additional burdens for smaller financial institutions that would take away from their ability to meet the needs of their borrowers and depositors. Participants in our industry and nonfederal banking regulator discussion groups noted that basic banking services and small-dollar loans are not always profitable and that further guidance will not solve that problem.

However, federal banking regulatory officials told us that they believed that their recent guidance does encourage institutions to make small-dollar consumer loans. They noted that they had provided additional guidance on small-dollar loan programs in the updated Q&As. The prior Q&As had noted that small, unsecured consumer loans provided in a safe and sound manner (i.e., based on the borrower's ability to repay) and with reasonable terms are an example of a lending activity that helps meet the credit needs of the community, and the updated Q&As issued in 2016 also stated that these products were an example of innovative or flexible lending.[81] However, respondents to our survey and participants in our discussion groups indicated the importance of additional CRA guidance after the issuance of these revised Q&As.

Treasury Plans Review of CRA Framework

In June 2017, Treasury announced plans to lead a review of how CRA is being implemented, though the agency did not have a timeline for completing this review. It identified the need for a review of CRA as part of its evaluation of existing laws and regulations required under Executive Order 13772.[82] Treasury noted the importance of modernizing the regulatory system to reflect how financial institutions currently do business while serving the financial needs of consumers.[83] Therefore, the agency announced it was planning a review of the CRA framework.

As noted previously, lower-income households were more likely to obtain credit or conduct financial transactions through an AFS provider and less likely to have a checking or savings account with a bank or credit union

[81]See *Interagency Questions and Answers Regarding Community Reinvestment* § __.22(a) – 1 and § __.22(b)(5) – 1. 81 Fed. Reg. 48506, 48536, 48538 (July 25, 2016).

[82]82 Fed. Reg. 9965 (Feb. 3, 2017).

[83]U.S. Department of the Treasury, *A Financial System That Creates Economic Opportunities: Banks and Credit Unions*.

than their higher-income counterparts. Further, lower-income households were more likely to be unbanked because they lacked sufficient funds, credit, or personal identification. Treasury's June 2017 report states that statutes of critical importance to the banking sector—including CRA—should better target the response to the risks that American consumers and the American economy face. The suggested options for improving how CRA is currently being implemented that our work identified are worth serious consideration as part of any evaluation of the CRA framework. Given the continuing unmet needs of LMI communities in obtaining basic banking services and small-dollar credit, consideration of these important options could help inform Treasury's review of the CRA framework and thereby further encourage financial institutions to provide these services and products.

Suggestions to Address Small-Dollar Loan Profitability and Safety and Soundness Concerns also Include Trade-Offs

Some stakeholders noted that institutions' concerns about profitability and safety and soundness may outweigh any perceived benefits of CRA ratings and play a larger role in whether they provide more small-dollar, nonmortgage consumer loans.[84] Some advocacy representatives noted that small-dollar loans are typically less profitable than alternative loan products financial institutions offer, such as overdraft protection programs. For example, one noted that small-dollar loans are not profitable due to underwriting standards and limits on interest rates. They also told us that financial institutions may be discouraged from making small-dollar consumer loans with interest rates greater than 36 percent because of perceived prohibitions against such rates, which further affects profitability.

Advocacy group representatives also observed that financial institutions that receive overdraft protection fee income may not want to lose this income by instead offering their customers lower-cost, small-dollar credit options that would directly compete with overdraft protection. Finally, advocacy and think tank representatives observed that unsecured, small-dollar loans can pose a risk to financial institutions because such loans typically have higher default rates. As a result, financial institutions may want to avoid offering products that may be deemed unsafe or unsound by the federal banking regulators.

[84]This section does not discuss basic banking services, as stakeholder concerns were primarily focused on small-dollar lending. However, some stakeholders noted that due to the typically low-dollar balances in accounts maintained by LMI individuals, financial institutions have concerns about the profitability of basic banking services as well.

Stakeholders suggested actions they believed the federal banking regulators could take to address profitability and safety and soundness concerns associated with offering small-dollar, nonmortgage consumer loans to LMI individuals. For example, they suggested loosening the underwriting requirements for loans under a certain dollar amount, thereby lowering the cost of originating such loans. However, advocacy group representatives noted that loosening underwriting requirements could be perceived as deregulation of the industry.

In addition, some think tank and industry representatives suggested that the federal banking regulators should clarify what is considered an acceptable interest rate for small-dollar consumer loans. They noted that the perception exists that financial institutions are not allowed to charge interest rates that are higher than 36 percent for small-dollar consumer loans, even if such rates would be much lower than those offered on payday loans. However, some industry group representatives believed it would be unlikely that the federal banking regulators would give CRA consideration for small-dollar loans with interest rates above 36 percent.

Some stakeholders also noted that minimizing compliance risk—risk arising from violations of, or nonconformance with, laws, rules, and regulations—would allow banks to offer profitable and safe small-dollar loans. For example, representatives from a think tank stated that financial institutions will not make small-dollar loans if they have to be fully underwritten, citing exposure to compliance risk if not done correctly. (For a more detailed discussion of these issues and other suggested options unrelated to CRA that address serving LMI consumers, see app. IV).

In commenting on these suggested actions, a federal banking regulator official noted that easing underwriting rules could be perceived as undermining safety and soundness. Further, officials with the federal banking regulators told us no federal laws authorize them to set the interest rates financial institutions may charge on small-dollar, nonmortgage consumer loans.[85] In 2007, FDIC issued guidance to the institutions it supervises on small-dollar loans that encourages an interest rate of no more than 36 percent.[86] However, FDIC officials noted this is

[85]The Military Lending Act, as implemented by the Department of Defense, prohibits creditors from offering most consumer credit at more than a 36 percent rate to service members and their families. See 10 U.S.C. 987.

[86]Federal Deposit Insurance Corporation, "Affordable Small-Dollar Loan Products: Final Guidelines," Financial Institution Letter (FIL)-50-2007 (Washington, D.C.: June 19, 2007).

merely guidance, not a regulation. Nonetheless, as noted previously, the perception of a 36 percent interest rate cap persists. Officials with FRB, FDIC, and OCC noted that CRA examiners, on a case by case basis, determine whether a loan program complies with applicable laws and is responsive to the community. They explained that a small-dollar consumer loan with an interest rate above 36 percent could receive positive CRA consideration, depending on other factors such as the context in which the loan was made, the communities in which the bank offered the loan, and the other types of programs available in the community. The officials stated that CRA examiners take all of these factors into consideration in making decisions about offering CRA consideration for small-dollar consumer loan programs, not simply the interest rate offered.

A new CFPB rule issued in November 2017 addresses some elements of acceptable small-dollar consumer loans, but its impact on financial institutions' willingness to make small-dollar, nonmortgage consumer loans is unclear.[87] In addition, financial technology (fintech) may enable firms to serve customers who are not profitable to serve using traditional means, and thus provide access to a range of products and services previously unavailable to them and on more affordable terms than high-

[87]On November 17, 2017, CFPB issued a final rule that, among other things, governs the underwriting of certain personal loans with short-term or balloon payment structures. See "Payday, Vehicle Title, and Certain High-Cost Installment Loan Rule," 82 Fed. Reg. 54472 (Nov. 17, 2017). According to CFPB, the rule is "aimed at stopping payday debt traps by requiring upfront whether consumers have the ability to repay their loans." Under the new rule, lenders that make short-term loans of 45 days or less or longer-term balloon payment loans generally must make an "ability-to-repay" determination, that is, must reasonably determine that the consumer will be able to make payments on the loan while also meeting major financial obligations and basic living expenses. (Loans made by a lender who makes 2,500 or fewer covered loans per year and derives no more than 10 percent of its revenue from such loans are exempt from the CFPB rule. According to CFPB, these are usually small personal loans made by community banks or credit unions to existing customers or members.) The rule also covers a third type of loan—loans with a term longer than 45 days with an APR over 36 percent that gives the lender account access. These loans are not subject to the ability-to-repay provisions but are subject to certain penalty fee prevention provisions. According to CFPB, these protections give consumers a chance to dispute any unauthorized or erroneous attempts by a lender to collect payment from the borrower's account and to arrange for unanticipated payments that are due. Since the compliance date for most provisions of the rule, including these provisions, is August 2019, its impact on banks' willingness to make small-dollar, nonmortgage consumer loans is not currently clear. CFPB recently released a statement that it intended to engage in a rulemaking process that reconsidered the payday rule.

cost alternatives such as payday loans.[88] For example, using alternative data may allow fintech lenders to offer loans to customers whose traditional credit history may not have been sufficient for banks to extend them credit. CFPB officials stated that using alternative data—including bill payment history as a proxy for debt repayment—could expand responsible access to credit, particularly to some individuals who are among the estimated 45 million people who lack traditional credit scores.

Conclusions

Treasury is planning to identify ways to improve the CRA framework in order to encourage financial institutions to better serve the financial needs of consumers. Our analysis has shown and Treasury recognizes that many LMI consumers' need for basic banking services and small-dollar loans is not being met by traditional financial institutions. For example, we found that although most LMI communities have as many banks and credit unions nearby as middle-income communities and the vast majority of Americans have a checking account, lower-income households are more likely to use costly AFS providers to meet their credit needs. Changes to CRA implementation we outlined could motivate financial institutions to make greater efforts to provide more of the low-cost services and loans LMI consumers are currently seeking outside the banking system. Giving careful consideration to these suggested options would help Treasury revise the current supervisory and regulatory framework to better align the benefits arising from financial institutions' CRA investments with the interest and needs of the communities that they serve, including the need for basic banking services and small-dollar consumer credit.

Recommendation for Executive Action

The Secretary of the Treasury should direct the Deputy Assistant Secretary for Small Business, Community Development & Housing Policy to consider the options that stakeholders have suggested for how CRA is implemented outlined in this report—such as revising the lending and service tests, expanding CRA to include all bank affiliates and nonbanks, expanding assessment areas, and issuing additional guidance—in the scope of the agency's planned review of the CRA framework.

[88]Financial technology, or "fintech," subsectors such as marketplace lending and mobile payments may provide consumers with additional options for accessing credit and banking services.

Agency Comments

We provided a draft of this report to Treasury, FRB, FDIC, and OCC for review and comment. In its written comments, reproduced in appendix V, Treasury stated that it concurred with our recommendation. FRB, FDIC, and OCC provided technical comments, which we incorporated as appropriate.

As agreed with your offices, unless you publicly announce the contents of this report earlier, we plan no further distribution until 30 days from the report date. At that time, we will send copies to Treasury, FRB, FDIC, and OCC. In addition, the report will be available at no charge on the GAO website at http://www.gao.gov.

If you or your staff have any questions concerning this report, please contact me at (202) 512-8678 or cackleya@gao.gov. Contact points for our Offices of Congressional Relations and Public Affairs may be found on the last page of this report. GAO staff who made major contributions to this report are listed in appendix VI.

Alicia Puente Cackley
Director, Financial Markets and
Community Investment

Appendix I: Objectives, Scope, and Methodology

This report examines (1) the availability of financial products and services to low- and moderate-income (LMI) consumers and their use of such financial products and services; (2) the extent to which Community Reinvestment Act (CRA) examinations evaluate financial institutions' provision of retail banking services; small-dollar, nonmortgage consumer loans; and support for community development in LMI communities; and (3) stakeholder views on options that could further encourage basic banking services and loans in LMI communities.[1]

To address our objectives, we reviewed the CRA statute and implementing regulations and interviewed knowledgeable officials with the federal banking regulators who oversee CRA: the Board of Governors of the Federal Reserve (FRB), Federal Deposit Insurance Corporation (FDIC), and Office of the Comptroller of the Currency (OCC). We also reviewed the Department of the Treasury's June 2017 report that describes its plan to conduct a review of the CRA framework.[2]

To assess the availability of financial products and services to LMI consumers and their use of such products and services, we used data from FDIC for 2016; the Federal Financial Institutions Examination Council (FFIEC) for 2014, 2015, and 2016; the National Conference of State Legislatures; the National Credit Union Administration (NCUA) for 2016; and the U.S. Census Bureau (Census) for 2010, 2014, and 2016 to estimate how the availability of basic banking services offered by banks, credit unions, and alternative financial services (AFS) providers in LMI communities compares to that in other communities.[3] (For technical details on our analysis of availability, see app. II.) We reviewed documentation on and conducted testing of the data we used and determined they were sufficiently reliable for the purpose of reporting on the availability of services offered by financial institutions and AFS providers. In addition, we analyzed data from FDIC's National Survey of

[1]Basic banking services are a subset of retail banking services, which is the term used in the CRA regulations and examination procedures. Basic banking services refers to those financial services needed to allow the average consumer to engage in necessary day-to-day banking activities. These services include deposit taking and simple transaction or savings account programs with low fees.

[2]U.S. Department of the Treasury, *A Financial System That Creates Economic Opportunities: Banks and Credit Unions* (Washington, D.C.: June 2017).

[3]AFS providers include transaction providers such as check cashing outlets and money transmitters, and credit providers such as payday loan stores, automobile title lenders, and pawnshop lenders.

Unbanked and Underbanked Households for 2011, 2013, and 2015 to estimate the relationship between household income and various financial behaviors and characteristics related to the use and accessibility of basic banking services and small-dollar loans. (For technical details on our household analysis, see app. III.) We reviewed documentation on and conducted testing of the data we used and determined they were sufficiently reliable for the purpose of reporting on how consumers' use of financial products and services vary with income.

To assess how the number of bank and credit union branches in the United States has changed nationwide in recent years, we examined data from FDIC on the number of bank branches in the 50 states and District of Columbia each year from 2005 to 2016 and from NCUA on the number of credit union branches each year from 2011 to 2016.[4] To assess how the number of AFS providers in the United States has changed in recent years, we examined County Business Patterns data from Census for 2005 to 2015 (the most recent data available). We used the number of establishments in North American Industry Classification System (NAICS) codes 522291 and 522390 to estimate the number of AFS establishments.[5] We reviewed documentation on and conducted testing of the data we used and determined they were sufficiently reliable for the purpose of reporting on the numbers of bank and credit union branches and AFS providers.

To determine the extent to which CRA examinations evaluate financial institutions' provision of (1) retail banking services, (2) small-dollar, nonmortgage consumer loans, and (3) support for community development in LMI communities, we reviewed the interagency CRA examination procedures for large, intermediate small, and small financial institutions. We identified those elements within the examination procedures that addressed our three topic areas and verified with each federal banking regulator that these elements were required to be

[4]NCUA data were not available prior to 2011.

[5]NAICS is the federal standard for classifying businesses by industry. NAICS code 522291 includes establishments primarily engaged in making unsecured cash loans to consumers such as finance companies, personal credit institutions, loan companies, and student loan companies. NAICS code 522390 includes establishments primarily engaged in facilitating credit intermediation such as check cashing services, money order issuance services, loan servicing, travelers' check issuance services, money transmission services, and payday lending services. While NAICS code 522390 appears to include all of the types of establishments that we consider AFS providers for the purpose of this report, we also included NAICS code 522291 to be consistent with other studies of AFS providers.

included in CRA public disclosure performance evaluations (performance evaluations). We included these examination elements in data collection instruments that we used to evaluate the contents of a sample of CRA performance evaluations. To develop these data collection instruments, we first composed questions and information items corresponding to our examination elements that were organized into a series of spreadsheets. We then tested these instruments on a small set of selected reports. Based on this test, refinements were made to the instruments before we undertook our full analysis. We selected a representative random sample of 219 CRA performance evaluations stratified by examination type—large, intermediate small, and small institution examinations. Our sampling frame was the list of all 1,273 CRA evaluations of large, intermediate small, and small institutions that were conducted in calendar year 2015 and published by July 19, 2016. We generated this list through searches on the federal banking regulators' websites. The final sample included 59 large, 76 intermediate small, and 84 small institution examinations. (See table 5.)

Table 5: Population and Sample of 2015 Community Reinvestment Act Performance Evaluations, by Examination Type

Examination type	Population	Sample
Large institution	150	59
Intermediate small institution	363	76
Small institution	760	84
Total	**1,273**	**219**

Source: GAO analysis of data from the Board of Governors of the Federal Reserve System, the Federal Deposit Insurance Corporation, and the Office of the Comptroller of the Currency. | GAO-18-244

Using our data collection instruments, we analyzed this sample of CRA performance evaluations to determine the extent to which they included evaluations of financial institutions' provision of retail banking services, small-dollar, nonmortgage consumer loans, and support for community development in LMI communities. We interviewed representatives of five financial institutions selected because their 2015 CRA performance evaluations mentioned consumer loans to obtain their perspectives on how such loans were assessed as part of the CRA examination. We also interviewed the CRA examiners who conducted the examinations for these five financial institutions to determine how the identified consumer loans were evaluated under CRA. Further, we reviewed CRA examiner training materials from each of the federal banking regulators to determine whether they included our three topic areas.

Because we followed a probability procedure based on random selections, our sample is only one of a large number of samples that we might have drawn. Since each sample could have provided different estimates, we express our confidence in the precision of our particular sample's results at a 95 percent confidence level. This is the interval that would contain the actual population value for 95 percent of the samples we could have drawn. As a result, we are 95 percent confident that each of the confidence intervals in this report will include the true values in the study population. The margin of error for all population estimates presented in each examination category (large, intermediate small, and small) is less than +/-11 percent at a 95 percent confidence level unless otherwise specified. Based on these procedures, we generated percentage estimates of the performance evaluations that included the examination elements related to our three topic areas.

To identify stakeholder views on options that could further encourage financial institutions to provide basic banking services and small-dollar, nonmortgage consumer loans to LMI consumers, we undertook a series of interconnected data collection steps. First, to identify an initial set of options, we conducted a literature search of databases that included general academic literature to identify publications from 2010 through 2015 that addressed our topics. The literature search results identified scholarly studies, policy briefs, news articles, and other sources that discussed options that could enhance financial inclusion. At the same time, and to supplement the literature review, we also held a series of interviews using questions that differed depending on the type of institution with 16 stakeholders to obtain their views on options that could further encourage financial institutions to provide basic banking services and small-dollar loans. These stakeholders included government agencies, industry associations, think tanks, and consumer advocacy organizations that were selected based on their knowledge on these matters. Second, we grouped the options we identified from both the literature review and interviews into a consolidated set of options for analysis.[6]

Third, to obtain initial information on the relative importance of these options, we administered an email survey from November 2016 through December 2016 to a non-generalizable sample of 66 individuals and organizations that were among the original sources of the options we

[6]We used an affinity mapping exercise to group the options for analysis.

identified and who agreed to participate in our survey. This sample included academics, advocacy and service groups, financial institutions or industry groups, government agencies, and think tanks. We also reached out to additional financial institutions to ensure representation across institution sizes in our survey.[7] We received survey responses from 31 of the 66 survey recipients. Despite the limitations inherent in this relatively low response rate, we determined that the number of responses we got were sufficient for us to make a general assessment about the relative importance of the options we identified. We conducted an analysis of our survey results to identify those options which were identified by respondents as most important, or key. Fourth, in January 2017 we held a series of five discussion groups with those survey respondents who were willing to participate to obtain their views on options that could encourage financial institutions to provide accessible and affordable basic banking services and small-dollar nonmortgage consumer loans in LMI communities. Although the views of these stakeholders were not necessarily representative of all stakeholders, their views offered important perspectives. To structure these discussion groups, we used our survey responses to identify and focus on each option from the survey identified as important.

We conducted this performance audit from August 2015 through February 2018 in accordance with generally accepted government auditing standards. Those standards require that we plan and perform the audit to obtain sufficient, appropriate evidence to provide a reasonable basis for our findings and conclusions based on our audit objectives. We believe that the evidence obtained provides a reasonable basis for our findings and conclusions based on our audit objectives.

[7]To ensure that our survey questions were clear and logical and that respondents could answer the questions without undue burden, we pretested our draft questionnaire with two individuals who were part of our sample. We then made changes to the questionnaire based on the pretest results.

Appendix II: Analysis of Availability of Financial Products and Services to Low- and Moderate-Income Communities

Data

We conducted an econometric analysis to assess how the availability of banking services to low- and moderate-income communities compares to that for other communities. We used data from the following sources:

- Federal Deposit Insurance Corporation (FDIC) for 2016;
- Federal Financial Institutions Examination Council (FFIEC) for 2014, 2015, and 2016;
- National Conference of State Legislatures as of September 2016;
- National Credit Union Administration (NCUA) for 2016; and
- Census Bureau (Census) for 2010, 2014, and 2016.

We defined communities as Census tracts and we used data from FFIEC to identify low-, moderate-, middle-, and upper-income tracts. FFIEC determines a tract's income group by comparing median family income in the tract to median family income in the metropolitan area or nonmetropolitan (rural) area of the state containing the tract (see table 6). This approach to identifying low-, moderate-, middle-, and upper-income tracts accounts for differences in purchasing power across metropolitan areas and rural areas in different states.

Table 6: Census Tract Income Group Definitions

(percent)

Census tract income	Median family income in the Census tract as a percentage of median family income in the metropolitan area or rural area of the state containing the tract
Low	Up to 49.9
Moderate	50 to 79.9
Middle	80 to 119.9
Upper	120 or more

Source: GAO analysis of data from the Federal Financial Institutions Examination Council. | GAO-18-244

In 2016, there were 73,057 Census tracts—60,903 in metropolitan areas and 12,154 in rural areas (see table 7). About 44 percent of all tracts were middle income, about 29 percent were low and moderate income, and about 26 percent were upper income. The remaining tracts were not assigned an income group, generally for reasons of confidentiality. Metropolitan areas were more likely to contain low- and moderate-income tracts than state rural areas. Overall, about 6 percent of the population

lived in low-income tracts in 2016 and about 21 percent of the population lived in moderate-income tracts.

Table 7: Numbers of Census Tracts and Percentage of Population in Census Tracts, by Income and Location Type, 2016

Census tract income	Number of Census tracts in:			Percentage of population in Census tracts in:		
	metropolitan areas	rural areas	all areas	metropolitan areas (percent)	rural areas (percent)	all areas (percent)
Low	5,338	170	**5,508**	5.9	0.2	**6.1**
Moderate	14,107	1,855	**15,962**	18.9	2.2	**21.1**
Middle	23,924	7,964	**31,888**	34.8	10.0	**44.8**
Upper	16,716	1,979	**18,695**	25.2	2.7	**27.8**
Unknown	818	186	**1,004**	0.2	<0.1	**0.3**
Total	**60,903**	**12,154**	**73,057**	**85.0**	**15.0**	**100**

Source: GAO analysis of data from the Federal Financial Institutions Examination Council. | GAO-18-244

Note: Totals may sum to more than 100 percent due to rounding.

We used data on tracts with at least 100 people for which demographic data and indicators of residential population density and land use were available for our analysis. Table 8 shows characteristics of tracts by income for metropolitan areas and rural areas for 2016.

Table 8: Characteristics of Census Tracts, by Income and Location Type, 2016

	Census tracts in metropolitan areas that are				Census tracts in rural areas that are			
	low income	moderate income	middle income	upper income	low income	moderate income	middle income	upper income
Average percentage of the population that is (percent):								
White	22.7	43.4	68.8	75.5	41.6	65.3	84.1	84.9
Hispanic	28.8	26.7	13.6	9.6	14.9	11.1	6.1	6.0
Black	41.2	22.2	10.1	5.7	28.8	15.6	6.1	5.8
Asian	4.1	4.4	4.6	6.6	1.0	0.7	0.7	0.9
Other race/ ethnicity	3.1	3.3	2.9	2.5	13.7	7.4	3.1	2.4
Female	51.2	51.0	51.1	51.1	51.4	50.6	50.0	50.0
Male	48.8	49.0	48.9	48.9	48.6	49.4	50.0	50.0
Age 17 & under	27.0	24.8	22.7	23.0	25.2	24.4	22.8	22.0
Age 18-24	14.6	11.7	9.3	8.0	19.2	10.1	8.3	8.5
Age 25-39	21.8	22.1	20.2	18.1	17.4	17.8	16.8	16.6
Age 40-49	12.2	13.0	14.1	15.5	11.1	12.8	13.5	13.9
Age 50-64	15.0	16.8	19.6	21.5	15.9	19.6	21.6	22.4
Age 65 & over	9.3	11.7	14.1	14.0	11.3	15.3	17.0	16.5
Average percentage of the population age 25 and over that has (percent):								
No high school diploma	32.0	23.6	13.0	6.1	31.4	24.7	17.0	12.2
High school diploma	32.0	32.3	30.4	19.2	33.6	37.7	38.3	32.1
Some college	23.2	27.0	30.2	27.0	23.6	25.8	28.4	29.6
Bachelor's degree or more	12.9	17.1	26.4	47.8	11.4	11.8	16.3	26.1
Average percentage of the population age 16 and over that is (percent):								
Employed	49.3	57.3	61.7	64.3	41.3	48.5	55.8	59.6
Unemployed	9.2	6.8	4.9	3.6	8.5	6.4	4.5	3.7
Not in labor force	41.5	35.9	33.4	32.0	50.2	45.2	39.7	36.7
Average percentage of homes that are (percent):								
Owner occupied	30.5	51.1	70.2	78.7	45.1	64.2	75.1	78.2
Rented/not owner occupied	69.5	48.9	29.8	21.3	54.9	35.8	24.9	21.8

	Census tracts in metropolitan areas that are				Census tracts in rural areas that are			
	low income	moderate income	middle income	upper income	low income	moderate income	middle income	upper income
Number of Census tracts that are:								
Rural	13	582	1,902	335	33	662	3,646	592
Mixed	349	2,356	8,022	5,957	73	880	3,786	1,276
Urban	4,968	11,166	13,992	10,415	64	313	530	107

Source: GAO analysis of data from the Federal Financial Institutions Examination Council. | GAO-18-244

Note: Census tracts are those in our analysis sample, which includes only tracts with at least 100 people for which demographic data and indicators of residential population density and land use were available.

Methodology

To compare the availability of banking services to low- and moderate-income communities to that for other communities, we estimated the parameters of econometric models with the following basic specification:

$$availability_c = \alpha + \beta low_c + \gamma moderate_c + \delta upper_c + X'_c\Theta + \varepsilon_c,$$

where c denotes the community; $availability_c$ is an indicator of the availability of banking services to community *c*; *low, moderate,* and *upper* are indicator variables equal to 1 if community *c* is low-income, moderate-income, or upper-income, respectively, and equal to 0 otherwise (so the omitted income group is middle); and X_c is a vector of other characteristics of community *c*. These other characteristics include indicators of population density and land use; the distribution of people with different demographic characteristics, such as age, race/ethnicity, gender, educational attainment, and labor force status; and the distribution of homes that are owner occupied or not. They also include metropolitan area and state rural area fixed effects to control for features that may vary across those areas but not across tracts within an area. The parameters of interest are β and γ. The parameter β measures the availability of banking services to low-income communities relative to middle-income communities, and the parameter γ measures the availability to moderate-income communities relative to middle-income communities.

We used three different approaches to estimating how the availability of banking services to low- and moderate-income communities compares to that for middle-income communities. As we explain below, the approaches differed in how we measured availability of banking services and in our geographic unit of analysis. However, all of our measures of availability of banking services are numbers that take only nonnegative

integer values. In addition, all of our specifications include fixed effects for metropolitan areas and state rural areas. To accommodate these features, we used fixed-effects Poisson regressions to estimate the parameters of the econometric models. We calculated robust standard errors to mitigate the effects of overdispersion in our measures of availability.

Analysis of Bank and Credit Union Branches Near Tracts

For our first approach, we used Census tracts as our unit of analysis and measured availability of banking services to people in a tract by counting the number of bank and credit union branches (hereafter, branches) within 2, 5, 10, and 25 miles of the tract. We identified the numbers of branches within these distances of each tract by geocoding the addresses of bank and credit union branches. Table 9 shows the average number of branches within 2, 5, 10, and 25 miles of tracts in our analysis sample by income in 2016.

Table 9: Numbers of Bank and Credit Union Branches Nearby Census Tracts with Different Income Levels, by Location Type, 2016

	Number of bank and credit union branches within the specified miles of											
	2 miles			5 miles			10 miles			25 miles		
	Mean	Min	Max	Mean	Min	Max	Mean	Min	Max	Mean	Min	Max
Census tracts in metropolitan areas that are												
Low income	27	0	463	130	0	1,046	375	0	1,966	1,050	0	4,245
Moderate income	18	0	471	91	0	1,051	279	0	1,964	854	0	4,253
Middle income	13	0	482	62	0	1,066	193	0	1,970	672	0	4,253
Upper income	18	0	487	82	0	1,056	243	0	1,964	879	0	4,253
Census tracts in rural areas that are												
Low income	6	0	25	11	0	37	15	0	49	49		51
Moderate income	4	0	25	7	0	46	10	0	62	62		48
Middle income	2	0	29	5	0	49	10	0	118	118		57
Upper income	2	0	29	6	0	42	15	0	115	115		75

Source: GAO analysis of data from the Census Bureau, the Federal Deposit Insurance Corporation, the Federal Financial Institutions Examination Council, and the National Credit Union Administration. | GAO-18-244

Note: Census tracts are those in our analysis sample, which includes only tracts with at least 100 people for which demographic data and indicators of residential population density and land use were available.

Table 10 shows the numbers of low-, moderate-, middle-, and upper-income tracts in our analysis sample with no branches within 2, 5, 10, and 25 miles in 2016. About 2 percent of low-income tracts, 10 percent of moderate-income tracts, 22 percent of middle-income tracts, and 16 percent of upper-income tracts had no branches within 2 miles. In rural areas, about 10 percent of low-income tracts, 10 percent of moderate-income tracts, 7 percent of middle-income tracts, and 6 percent of upper-income tracts had no branches within 10 miles.

Table 10: Number of Census Tracts with No Bank and Credit Union Branches Nearby, by Income Level and Location Type, 2016

	Metropolitan areas					Rural areas				
	Number of Census tracts with no branches within				Total tracts	Number of Census tracts with no branches within				Total tracts
	2 miles	5 miles	10 miles	25 miles		2 miles	5 miles	10 miles	25 miles	
Low income	89	24	13	2	**5,330**	52	34	18	6	**170**
Moderate income	1,403	499	119	22	**14,104**	934	509	179	37	**1,855**
Middle income	5,352	1,594	255	25	**23,916**	5,280	2,624	587	62	**7,962**
Upper income	2,707	457	72	7	**16,707**	1,303	572	124	14	**1,975**

Source: GAO analysis of data from the Census Bureau, the Federal Deposit Insurance Corporation, the Federal Financial Institutions Examination Council, and the National Credit Union Administration. | GAO-18-244

Note: Census tracts are those in our analysis sample, which includes only tracts with at least 100 people for which demographic data and indicators of residential population density and land use were available.

Analysis of Large Bank Community Reinvestment Act Assessment Areas Containing Tracts

For the second approach, we measured the availability of banking services using the number of banks with assets of about $1.2 billion or more (hereafter, large banks) that included the tract in its Community Reinvestment Act (CRA) assessment area. A bank's assessment area includes the geographies where it has its main office, its branches, and its deposit-taking automated teller machines, as well as the surrounding geographies in which the bank has originated or purchased a substantial portion of its loans. In 2015, low-income tracts in metropolitan areas were contained in 24 large bank assessment areas on average and moderate-income tracts were contained in 22 (see table 11). Middle- and upper-income tracts in metropolitan areas were contained in 19 and 24 assessment areas, on average. Tracts in rural areas were contained in fewer assessment areas—low-, moderate-, and middle-income tracts were contained in 4 on average and upper-income tracts were contained in 5.

Table 11: Number of Large Bank Community Reinvestment Act Assessment Areas Containing Census Tracts, by Income and Location Type, 2015

	Number of large bank assessment areas containing Census tracts in metropolitan areas that are:				Number of large bank assessment areas containing Census tracts in rural areas that are:			
	low income	moderate income	middle income	upper income	low income	moderate income	middle income	upper income
Mean	24	22	19	24	4	4	4	5
Minimum	0	2	0	0	0	0	0	0
Maximum	62	62	62	62	10	11	12	12

Source: GAO analysis of data from the Federal Financial Institutions Examination Council. | GAO-18-244

Analysis of Alternative Financial Services Establishments in Counties

For the third approach, we used counties as the unit of analysis and measured the availability of banking services using numbers of alternative financial services (AFS) establishments in counties. Table 12 shows the average numbers of bank and credit union establishments and AFS establishments in counties in 2014. For this approach, we aggregated tract-level information up to the county level so that the variables *low, moderate,* and *upper* in our econometric model measure the share of county population in low-, moderate-, and upper-income tracts, respectively. It follows that the parameters of interest, β and γ, are estimates of the relative change in the number of establishments associated with a 1 percentage point increase in the share of county population that lives in low- and moderate-income communities, respectively.

Table 12: Number of Alternative Financial Services Establishments per 10,000 People in Counties, by Location Type, 2014

	Numbers of alternative financial services establishments per 10,000 people in counties in:	
	metropolitan areas	rural areas
Mean	20	3
Minimum	0	0
Maximum	858	48

Source: GAO analysis of data from the Census Bureau and the Federal Financial Institutions Examination Council. | GAO-18-244

Notes: Numbers of establishments are from the County Business Patterns. Alternative financial services establishments are those with North American Industry Classification System codes 522291 and 522390.

Each of these three approaches sheds light on different aspects of the availability of banking services to a community. In our first approach, the

measures of availability—numbers of bank and credit union branches within 2, 5, 10, and 25 miles of a tract—reflect a community's physical proximity to branches of banks and credit unions of all sizes. The measure of availability we used in our second measure—numbers of large bank assessment areas containing a tract—allows large banks to self-identify the geographic area they generally serve and thus may more accurately measure availability of banking services in a community than the first measure. On the other hand, this measure is only available for banks with assets of about $1 billion or more, so it understates the availability of banking services in a community to the extent that services provided by smaller banks or credit unions are also available. Finally, our third approach—estimating the relationship between the number of AFS establishments in a county and the distribution of county population across low-, moderate-, middle-, and upper-income communities—sheds light on the availability of banking services provided by nonbanks. However, this approach may overstate the availability if establishments are not distributed uniformly across counties and if counties are large relative to the tracts they contain.

The descriptive statistics in the tables above suggest that metropolitan areas and state rural areas may be different, so we obtain estimates using the full sample of tracts and counties, using only tracts and counties in metropolitan areas, and using only tracts and counties in rural areas of states. For our analysis of bank and credit union branches near tracts, we also obtain estimates using only tracts in metropolitan areas of different sizes and in each of the largest 25 metropolitan areas.

Caveats and Limitations

Our analysis has limitations and our results should be interpreted with caution. For example, our analysis does not establish causal relationships between community income and availability of basic banking services. In addition, our results may not generalize to other time periods, and they may not represent the experience of any one community in particular. Furthermore, our estimates of the relationship between availability and income may also reflect factors other than income. We controlled for several characteristics that may be associated with availability and also correlated with income, such as race/ethnicity, educational attainment, and the homeownership rate. However, we may not have controlled for all possible characteristics that are associated with availability. If a characteristic we omitted is associated with income, then our results may reflect the relationship between availability and this omitted factor instead of, or in addition to, the relationship between availability and income. There may be alternative measures of availability other than the ones we

used, and these measures may produce different results. Finally, geographic proximity is only one aspect of the availability of basic banking services to a community. Other aspects of availability may also play a role in whether or not people in a community have access to banking services, and some people in a community may not have access to banking services even if a financial institution is located nearby.

Results

Analysis of Bank and Credit Union Branches Near Tracts

Our analysis suggests that low-income communities have more bank and credit union branches nearby than middle-income communities in some types of locations but the same or less in others. In 2016, the number of bank and credit union branches within 2 miles of low-income tracts was greater on average than the number within 2 miles of middle-income tracts in metropolitan areas with 250,000 to 499,999 people, in metropolitan areas with 500,000 to 999,999 people, and in metropolitan areas with 1 million people or more, all else—including the demographic characteristics of the tract, its population density and land use category, and the metropolitan area where it was located—being equal (see table 13). The difference in the number of branches within 2 miles of low- and middle-income tracts was greater in larger metropolitan areas—about 11 percent greater in metropolitan areas with 250,000 to 499,999 people, about 22 percent greater in metropolitan areas with 500,000 to 999,999 people, and about 31 percent in metropolitan areas 1 million people or more. However, the number of branches within 2 miles of low-income tracts was not statistically significantly different from the number within 2 miles of middle-income tracts in metropolitan areas with 100,000 to 249,999 people, and it was about 35 percent less in metropolitan areas with 99,999 people or fewer. The number of branches within 2 miles of low-income tracts was not statistically significantly different from the number within 2 miles of middle-income tracts in rural areas of states. Finally, for each of the largest 25 metropolitan areas, we generally found that the number of branches within 2 miles of low-income tracts was either greater than or not significantly different from the number within 2 miles of middle-income tracts.

Table 13: Ratio of Bank and Credit Union Branches Nearby Low, Moderate-, and Upper-Income Census Tracts to Branches Nearby Similar Middle-Income Tracts, by Location Type, 2016

	Estimated ratio of the number of bank and credit union branches within 2 miles of low-, moderate-, and upper-income Census tracts to the number within 2 miles of similar middle-income tracts in the same area, in:							
	all areas	all metropolitan areas	metropolitan areas with:					rural areas
			1 million people or more	500,000 to 999,999 people	250,000 to 499,999 people	100, 000 to 249,999 people	99,999 people or fewer	
Ratio for low-income tracts	1.28[a]	1.28[a]	1.31[a]	1.22[a]	1.11[b]	1.09	0.65[b]	0.90
	(0.03)	(0.03)	(0.03)	(0.06)	(0.06)	(0.06)	(0.14)	(0.07)
Ratio for moderate-income tracts	1.10[a]	1.10[a]	1.10[a]	1.10[a]	1.10[a]	1.07[b]	1.04	1.03
	(0.03)	(0.03)	(0.03)	(0.04)	(0.04)	(0.04)	(0.09)	(0.04)
Ratio for upper-income tracts	1.01	1.01	1.00	0.98	1.08b	1.07[c]	0.86	1.10[b]
	(0.04)	(0.04)	(0.04)	(0.05)	(0.03)	(0.04)	(0.11)	(0.05)
Number of tracts	72,019	60,057	39,004	8,381	6,280	5,798	594	11,962
Number of areas	449	402	73	54	80	166	29	47
Log likelihood	-334,438	-309,928	-233,870	-32,418	-21,371	-17,452	-1,727	-21,749

Source: GAO analysis of data from the Census Bureau, the Federal Deposit Insurance Corporation, the Federal Financial Institutions Examination Council, and the National Credit Union Administration. | GAO-18-244

Notes: The table shows the exponentiated coefficient estimates from Poisson regressions of the number of bank and credit union branches within 2 miles of Census tracts on indicators of tract income. The regressions also controlled for tract population density and land use category; the demographic mix of tract population by age, race/ethnicity, gender, educational attainment, and labor force status; the mix of homes in the tract by homeownership status; and the metropolitan area or rural area of the state where the tract is located. The omitted income group is middle income. All else being equal, the estimated average ratio of the number of branches nearby low-, moderate-, and upper-income tracts to the number nearby middle-income tracts is approximately equal to the reported exponentiated coefficient estimate. Robust standard errors are in parentheses.

[a]Statistically significant at the 1 percent level.

[b]Statistically significant at the 5 percent level.

[c]Statistically significant at the 10 percent level.

Our analysis also suggests that moderate-income communities also have more bank and credit union branches nearby than middle-income communities in some areas and the same or less in others. In 2016, the number of branches within 2 miles of moderate-income tracts was about 7 to 10 percent greater than the number within 2 miles of middle-income tracts in metropolitan areas with 100,000 people or more. However, in metropolitan areas with 99,999 people or fewer and in rural areas of

states, the number of branches within 2 miles of moderate-income tracts was not statistically significantly different from the number within 2 miles of middle-income tracts. Finally, for each of the 25 largest metropolitan areas, we found that the number of branches within 2 miles of moderate-income tracts was greater than or not statistically different from the number within 2 miles of moderate-income tracts for most of the 25 largest metropolitan areas, but was less than the number within 2 miles of middle-income tracts in a few (see table 14).

Table 14: Ratio of Bank and Credit Union Branches Nearby Low-, Moderate-, and Upper-Income Census Tracts to Branches Nearby Similar Middle-Income Tracts, by Metropolitan Area, 2016

	Estimated ratio of the number of bank and credit union branches within 2 miles of a Census tract to the number within 2 miles of similar middle-income tracts, for tracts in metropolitan area that are:			Number of Census tracts in metropolitan area	Log likelihood
Metropolitan area	**low income**	**moderate income**	**upper income**		
1. New York-Newark-Jersey City, NY-NJ-PA	1.085	1.067	1.039	4,604	-59,979.1
	(0.069)	(0.045)	(0.044)		
2. Los Angeles-Long Beach-Anaheim, CA	1.209[a]	0.944[c]	1.110[a]	2,887	-16,134.6
	(0.073)	(0.032)	(0.036)		
3. Chicago-Naperville-Elgin, IL-IN-WI	1.184[c]	1.025	1.097[c]	2,201	-13,553.4
	(0.118)	(0.057)	(0.061)		
4. Dallas-Fort Worth-Arlington, TX	1.304[a]	1.007	0.859[a]	1,320	-5,311.9
	(0.130)	(0.066)	(0.049)		
5. Houston-The Woodlands-Sugar Land, TX	1.310[b]	1.090	0.880[c]	1,062	-4,550.86
	(0.144)	(0.087)	(0.059)		
6. Washington-Arlington-Alexandria, DC-VA-MD-WV	1.204	1.179[c]	0.974	1,346	-10,166.2
	(0.195)	(0.113)	(0.083)		
7. Philadelphia-Camden-Wilmington, PA-NJ-DE-MD	1.020	0.931	1.324[a]	1,457	-8,635.85
	(0.116)	(0.062)	(0.078)		
8. Miami-Fort Lauderdale-West Palm Beach, FL	1.150	1.057	0.984	1,190	-6,621.47
	(0.126)	(0.058)	(0.054)		
9. Atlanta-Sandy Springs-Roswell, GA	1.770[a]	1.160[c]	1.018	945	-3,264.74
	(0.227)	(0.098)	(0.090)		
10. Boston-Cambridge-Newton, MA-NH	1.217	1.051	1.299[a]	988	-6,434.16
	(0.149)	(0.081)	(0.082)		
11. San Francisco-Oakland-Hayward, CA	1.165	0.979	1.118[c]	969	-6,693.24
	(0.118)	(0.068)	(0.074)		

Metropolitan area	Estimated ratio of the number of bank and credit union branches within 2 miles of a Census tract to the number within 2 miles of similar middle-income tracts, for tracts in metropolitan area that are: low income	moderate income	upper income	Number of Census tracts in metropolitan area	Log likelihood
12. Phoenix-Mesa-Scottsdale, AZ	1.114	1.027	0.932	980	-3,471.33
	(0.114)	(0.060)	(0.060)		
13. Riverside-San Bernardino-Ontario, CA	1.024	0.948	1.179[b]	817	-2,414.15
	(0.137)	(0.067)	(0.094)		
14. Detroit-Warren-Dearborn, MI	1.131	0.974	1.043	1,282	-4,956.02
	(0.107)	(0.056)	(0.047)		
15. Seattle-Tacoma-Bellevue, WA	1.294[c]	1.146[c]	1.202[a]	717	-3,373.95
	(0.176)	(0.087)	(0.082)		
16. Minneapolis-St. Paul-Bloomington, MN-WI	1.025	0.823[a]	1.106	785	-2,665.07
	(0.118)	(0.053)	(0.085)		
17. San Diego-Carlsbad, CA	1.337[a]	1.099	0.940	622	-2,516.61
	(0.124)	(0.070)	(0.066)		
18. Tampa-St. Petersburg-Clearwater, FL	1.184	0.959	0.941	733	-3,234.53
	(0.181)	(0.077)	(0.089)		
19. Denver-Aurora-Lakewood, CO	0.929	0.836[b]	0.986	614	-2,495.46
	(0.117)	(0.071)	(0.072)		
20. St. Louis, MO-IL	1.062	0.935	1.002	613	-2,118.88
	(0.146)	(0.072)	(0.078)		
21. Baltimore-Columbia-Towson, MD	1.349[a]	1.019	0.880	671	-2,770.95
	(0.139)	(0.066)	(0.072)		
22. Charlotte-Concord-Gastonia, NC-SC	0.899	0.858	0.763[b]	534	-1,636.72
	(0.155)	(0.096)	(0.100)		
23. Orlando-Kissimmee-Sanford, FL	1.451	1.253[b]	1.043	388	-1,386.13
	(0.344)	(0.129)	(0.086)		
24. San Antonio-New Braunfels, TX	1.451[b]	1.334[a]	0.976	453	-1,547.17
	(0.212)	(0.132)	(0.098)		
25. Portland-Vancouver-Hillsboro, OR-WA	1.057	1.049	1.008	488	-1,934.11
	(0.146)	(0.072)	(0.074)		

Source: GAO analysis of data from the Census Bureau, the Federal Deposit Insurance Corporation, the Federal Financial Institutions Examination Council, and the National Credit Union Administration. | GAO-18-244

Notes: The table shows the exponentiated coefficient estimates from Poisson regressions of the number of bank and credit union branches within 2 miles of Census tracts on indicators of tract income. The regressions also controlled for tract population density and land use category; the demographic mix of tract population by age, race/ethnicity, gender, educational attainment, and labor force status; the mix of homes in the tract by homeownership status; and the metropolitan area or rural area of the state where the tract is located. The omitted income group is middle income. All else being equal, the estimated average ratio of the number of branches nearby low-, moderate-, and

upper-income tracts to the number nearby middle-income tracts is approximately equal to the reported exponentiated coefficient estimate. Robust standard errors are in parentheses.

[a]Statistically significant at the 1 percent level.

[b]Statistically significant at the 5 percent level.

[c]Statistically significant at the 10 percent level.

We also found that the numbers of branches within 5 miles of low- and moderate-income tracts were also greater than the numbers within 5 miles of middle-income tracts for metropolitan areas with 100,000 to 249,999 people, metropolitan areas with 250,000 to 499,999 people, metropolitan areas with 500,000 to 999,999 people, and metropolitan areas with 1 million people or more, and also for rural areas of states. For metropolitan areas with 99,999 people or fewer, the numbers of branches nearby low- and moderate-income tracts were not statistically significantly different from the numbers nearby middle-income tracts. Finally, we found that the numbers of branches within 10 miles of low- and moderate-income tracts were greater than the numbers within 10 miles of middle-income tracts in rural areas and in metropolitan areas with at 100,000 to 999,999 people, but not in metropolitan areas with 99,999 people or fewer or in metropolitan areas with 1 million or more people. Altogether, these patterns suggest that banks and credit unions are more available to low- and moderate-income communities than they are to similar middle-income communities in some areas, but are equally or less available in others.

Analysis of Large Bank Community Reinvestment Act Assessment Areas Containing Tracts

Our analysis of large bank assessment areas suggests that the number of large bank assessment areas containing low- and moderate-income tracts in metropolitan areas is no greater than the number containing similar middle-income tracts in the same area (see table 15). In 2015, low-income tracts in metropolitan areas were contained in about the same number of large bank assessment areas as middle-income tracts in the same areas, while moderate-income tracts are contained in about 1 percent fewer. Our estimates also suggest, however, that the number of large bank assessment areas containing low- and moderate-income tracts in rural areas is at least as great as the number containing middle-income tracts in the same area. Low-income tracts in rural areas were contained in about 1.1 times as many large bank assessment areas as similar middle-income tracts in the same rural area. Altogether, these estimates suggest that banking services provided by large banks are no more available to low- and moderate-income communities in metropolitan areas than they are to similar middle-income communities in the same area, and possibly less, while banking services provided by large banks

are at least as available to low- and moderate-income communities in rural areas of states as they are to similar middle-income communities in the same area, and possibly more.

Table 15: Ratio of Number of Large Bank Community Reinvestment Act Assessment Areas Containing Low-, Moderate-, and Upper-Income Census Tracts to Number Containing Similar Middle-Income Tracts, 2015

	Estimated ratio of the number of large bank assessment areas containing low-, moderate-, and upper-income Census tracts to the number containing similar middle-income tracts in:		
	all areas	**all metropolitan areas**	**rural areas**
Ratio for low-income tracts	0.991	0.987	1.131[a]
	(0.017)	(0.016)	(0.054)
Ratio for moderate-income tracts	0.988[b]	0.988[b]	1.029
	(0.005)	(0.004)	(0.021)
Ratio for upper-income tracts	1.010	1.006	1.064[a]
	(0.011)	(0.011)	(0.028)
Number of tracts	72,019	60,045	11,974
Number of areas	448	401	47
Log likelihood	-181,546	-157,620	-23,413

Source: GAO analysis of data from the Federal Financial Institutions Examination Council. | GAO-18-244

Notes: The table shows the exponentiated coefficient estimates from Poisson regressions of the number of large bank assessment areas containing Census tracts on indicators of tract income. The regressions also controlled for tract population density and land use category; the demographic mix of tract population by age, race/ethnicity, gender, educational attainment, and labor force status; the mix of homes in the tract by homeownership status; and the metropolitan area or rural area of the state where the tract is located. The omitted income group is middle income. All else being equal, the estimated average ratio of the number of large bank assessment areas containing low-, moderate-, and upper-income tracts to the number containing middle-income tracts is approximately equal to the reported exponentiated coefficient estimate. Robust standard errors are in parentheses.

[a]Statistically significant at the 5 percent level.

[b]Statistically significant at the 1 percent level.

Analysis of Alternative Financial Services Establishments in Counties

Our analysis suggests that small changes in the share of people in moderate-income tracts are not associated with statistically significant changes in the number of AFS establishments (see table 16). However, a small increase in the share of people in low-income tracts is associated with a reduction in the number of AFS establishments in the county. Specifically, a 1 percentage point increase in the share of people in low-income tracts is associated with about a 1 percent reduction in the number of AFS establishments in a county, all else being equal. Estimated changes in the numbers of AFS establishments in specific groups of counties—those that do not prohibit payday lending, those in metropolitan areas, and those in state rural area—associated with similar

changes in the share of people in low- and moderate-income tracts are similar. The one exception is for counties in states that prohibit payday lending. For counties in these states, the number of AFS establishments appears to be unrelated to the share of county population in low- and moderate-income tracts.

Table 16: Changes in Alternative Financial Services Establishments in Counties Associated with Changes in Population in Low-, Moderate-, and Upper-Income Census Tracts, 2014

	Estimated ratio of the number of alternative financial services establishments in a county to the number in a similar county with 1 percentage point less population in low-, moderate-, and upper-income tracts for:				
	all counties	counties in:			
		states that do not prohibit payday lending	states that prohibit payday lending	metropolitan areas	rural areas
Ratio for population in low-income tracts	0.988[a]	0.988[a]	1.000	0.987[b]	0.990[a]
	(0.003)	(0.003)	(0.010)	(0.005)	(0.002)
Ratio for population in moderate-income tracts	1.001	1.001	1.003	1.002	1.000
	(0.001)	(0.001)	(0.005)	(0.002)	(0.002)
Ratio for population in upper-income tracts	1.000	1.000	1.003	1.004	0.998[a]
	(0.001)	(0.001)	(0.002)	(0.003)	(0.001)
Number of counties	2,974	2,633	332	1003	1,971
Number of areas	286	254	35	241	45
Log likelihood	-4,510	-3,872	-426	-1,874	-2,549

Source: GAO analysis of data from the Census Bureau and the Federal Financial Institutions Examination Council. | GAO-18-244

Notes: The table shows the exponentiated coefficient estimates from Poisson regressions of the number of alternative financial services establishments in counties on the fractions of county population in low-, moderate-, and upper-income Census tracts. The regressions also controlled for county population; the fractions of county population in tracts by population density and land use category; the distribution of county population across different groups by race/ethnicity, gender, age, education, and labor force status; the fraction of housing stock that is owner-occupied; and the metropolitan area or rural area of the state where the county is located. The omitted income group is middle income. All else being equal, the estimated average ratio of the number of establishments in a county to the number of establishments in a county with 1 percentage point less population in low-, moderate-, and upper-income tracts is approximately equal to the reported exponentiated coefficient estimate. Robust standard errors are in parentheses.

[a]Statistically significant at the 1 percent level.

[b]Statistically significant at the 5 percent level.

Appendix III: Econometric Analysis of Household Income and Use of Financial Products and Services

Data

To assess the extent to which household use of financial products and services varies with income, we used data from the Federal Deposit Insurance Corporation's National Survey of Unbanked and Underbanked Households for 2011, 2013, and 2015. To assess the use and accessibility of basic banking services for households with different incomes, we used data on whether or not households:

- Had a checking or savings account at the time of the survey,
- Used alternative financial services (AFS) providers for transactions, such as money orders or check-cashing, in the past 12 months,
- Used general-purpose reloadable prepaid cards in the past 12 months,
- Typically received income and paid bills using methods associated with checking or savings accounts in the past 12 months,
- Used direct deposit in the past 12 months,
- Used a bank teller, automated teller machine (ATM) or bank kiosk, telephone banking, online banking, or mobile banking to access their account in the past 12 months (households with checking or savings accounts only),
- Did not have a checking or savings account because bank hours or locations are inconvenient, because bank account fees are too high or unpredictable, because banks do not offer needed products or services, because they do not trust banks, because they do not have enough money to keep in an account, because avoiding banks provides more privacy, or because they cannot open an account due to personal identification, credit, or former bank account problems (only households that do not have a checking or savings account).

See table 17 for the distribution of values of these variables for households in 2015.

Table 17: Household Responses to Questions Related to Basic Banking Services, 2015

(percent)

	Yes	No	Do not know or refused to answer
Estimated percentage of households that:			
Have a checking or savings account at the time of the survey	93.0	7.0	0
Used alternative financial services providers for transactions within the past 12 months	20.2	74.2	5.6
Used general-purpose reloadable prepaid cards within the past 12 months	9.8	85.8	4.4
Typically received income and paid bills using methods associated with checking or savings accounts in the past 12 months	70.5	29.5	0
Used direct deposit in the past 12 months	80.4	19.6	0
Estimated percentage of households with a checking or savings account that accessed it in the past 12 months using:			
Bank teller	75.5	24.5	0
Automated teller machine or kiosk	69.8	30.2	0
Telephone banking	27.0	73.0	0
Online banking	60.4	39.6	0
Mobile banking	31.9	68.1	0
Estimated percentage of households that do not have a checking or savings account because:			
Bank hours or locations are inconvenient	12.6	83.2	4.2
Bank account fees are too high or unpredictable	31.6	63.3	5.2
Banks do not offer needed products or services	15.4	79.1	5.5
They do not trust banks	28.0	66.4	5.6
They do not have enough money to keep in an account	57.4	36.8	5.9
Avoiding banks provides more privacy	28.5	65.1	6.4
They have personal identification, credit, or former bank account problems	16.4	76.9	6.6

Source: GAO analysis of data from the Federal Deposit Insurance Corporation. | GAO-18-244

Notes: The sample size is 36,189, representing a population of about 127.5 million. Of the households sampled, 32,491 had a checking or savings account, representing a population of about 113.3 million. Similarly, 2,275 households sampled did not have either a checking or a savings account, representing a population of about 9.0 million.

To assess the demand for and access to small-dollar, unsecured credit for households with different incomes, we used data on whether or not households:

- Used nonbanks or AFS providers for credit, such as payday loans, auto title loans, pawnshop loans, and tax refund anticipation loans, in the past 12 months,
- Used credit cards in the past 12 months,
- Had a personal loan or line of credit at a bank in the past 12 months,
- Desired consumer credit in the past 12 months—applied for a new credit card or personal loan or line of credit at a bank (excluding student loans or loans taken out for major purchases like a house or car), or wanted to but did not for fear of being turned down,
- Were consumer credit constrained in the past 12 months—applied for a new credit card or personal loan or line of credit from a bank and were partially or fully turned down, or wanted a new credit card or a personal loan or line of credit from a bank but did not apply for fear of being turned down,
- Set aside money for unexpected expenses or emergencies in the past 12 months,
- Fell behind on bills in the past 12 months.

See table 18 for the distribution of values of these variables for households in 2015.

Table 18: Household Responses to Questions Related to Small-Dollar, Unsecured Loans, 2015

(percent)

Estimated percentage of households that, in the past 12 months:	Yes	No	Do not know or refused to answer
Used nonbanks or alternative financial services providers for credit	7.7	86.9	5.5
Used credit cards	66.5	33.5	0
Had a personal loan or line of credit at a bank	9.8	90.2	0
Desired consumer credit	16.8	75.5	7.7
Were consumer credit constrained	7.0	75.5	17.5
Set aside money for unexpected expenses or emergencies	56.3	43.7	0
Fell behind on bills	15.6	76.9	7.5

Source: GAO analysis of data from the Federal Deposit Insurance Corporation. | GAO-18-244

Notes: The sample size is 36,189, representing a population of about 127.5 million. A household desired consumer credit if it applied for a new credit card or personal loan or line of credit at a bank (excluding student loans or loans taken out for major purchases like a house or car), or wanted to but did not for fear of being turned down. A household was credit constrained if it applied for a new credit card or personal loan or line of credit from a bank and was partially or fully turned down, or wanted a new credit card or a personal loan or line of credit from a bank but did not apply for fear of being turned down.

Methodology

For each of the financial behaviors and characteristics of households listed above, we estimated the relationship between household income and the likelihood that a household exhibited the behavior or had the characteristic. Specifically, for each behavior or characteristic listed above, we estimated the parameters of the following type of econometric model:

$$Prob(y=1) = \alpha + \beta(\text{income } \$14{,}999 \text{ or less}) + \chi(\text{income } \$15{,}000\text{-}29{,}999) + \delta(\text{income } \$30{,}000\text{-}49{,}999) + \phi(\text{income } \$50{,}000\text{-}74{,}999) + X'\Theta + \varepsilon,$$

where y=1 if a household exhibits the behavior or has the characteristic and y=0 otherwise; X is a vector of characteristics of households and heads of households other than income; $\alpha, \beta, \chi, \delta, \phi$ and Θ are parameters to be estimated; and ε is an error term.

To measure income, we used indicator variables that are equal to 1 if household income is in a given interval and equal to 0 otherwise—$14,999 or less, from $15,000 to $29,999, from $30,000 to $49,999, and from $50,000 to $74,999. The reference group is households with income

of $75,000 or more. With this setup, the parameters of interest—β, χ, δ, and ϕ—show the effects of the income groups on the likelihoods that households exhibit a behavior or have a characteristic relative to households with income of $75,000 or more. For example, if *y* indicates whether or not a household has a checking or savings account, then the parameter β is the likelihood that households with income of $14,999 or less have a checking or savings account relative to households with income of $75,000 or more, all else being equal. If β is less than zero, then households with income of $14,999 or less are less likely to have a checking or savings account than households with $75,000 or more, and vice versa.

Our approach to measuring household income allows the relationship between income and the probability that a dependent variable equals 1 to be nonlinear. As a practical matter, income is measured this way in the raw data.

The characteristics of households and household heads other than income generally include household type, homeownership status, language, age, education, employment, nativity and citizenship, race/ethnicity, location (either region or metropolitan area or rural area of a state), and location type. We use groups of indicator variables to control for all of these characteristics. Table 19 summarizes the characteristics of households and heads of households in our data for 2015.

Table 19: Characteristics of Households and Heads of Households, 2015

Household characteristics (estimated percentage of households)	
Income	
Less than $15,000	14.1
$15,000 to $29,999	16.8
$30,000 to $49,999	19.9
$50,000 to $74,999	18.0
$75,000 or more	31.2
Household type	
Married couple	46.7
Unmarried female-headed family	12.5
Unmarried male-headed family	4.8
Female individual	18.4
Male individual	17.3
Other	0.2
Homeownership status	
Homeowner	63.3
Nonhomeowner	36.7
Language spoken at home	
Spanish only	2.2
Not Spanish only	97.8
Location type	
Metropolitan area – principal city	28.6
Metropolitan area – balance	42.8
Not in metropolitan area	14.0
Not identified	14.5
Region	
Northeast	17.8
Midwest	21.7
South	37.9
West	22.6

Head of household characteristics (estimated percentage of heads of households)	
Age	
15-24 years	5.2
25-34 years	16.5
35-44 years	17.0
45-54 years	18.6
55-64 years	18.8
65 years and over	23.9
Education	
No high school diploma	10.8
High school diploma	26.1
Some college	29.4
College degree	33.7
Labor force status	
Employed	61.3
Unemployed	3.0
Not in labor force	35.7
Nativity and citizenship	
U.S.-born	85.2
Foreign-born citizen	7.6
Foreign-born non-citizen	7.2
Race/ethnicity	
Black	14.1
Hispanic	12.6
Asian	4.9
White	67.0
Other	1.4
Sample size	**36,189**
Population	**127.5 million**

Source: GAO analysis of data from the Federal Deposit Insurance Corporation. | GAO-18-244

Notes: The data also include information on the state and metropolitan area in which households live. We do not report summary statistics for these variables for brevity.

We collapsed the responses “no” and “don’t know/refused” into a single category for our regression analysis, so the dependent variables are all binary indicator variables.

We derived our baseline estimates from linear probability models that account for the survey features of the data. We estimated separate regressions for each dependent variable listed in tables 17 and 18 using data for 2015, and also using data for 2011 and 2013 when possible. We estimated the parameters of three specifications: (1) one with income as the only explanatory variable, (2) one with the full set of explanatory variables listed in table 19, and (3) one with the full set of explanatory variables listed in table 19 but with indicators for metropolitan areas and rural areas of states instead of region indicators.

We started with the linear probability model as a practical option that balances the ability to account for the survey features of the data with the processing time it takes to estimate the parameters, especially in a model with explanatory variables that are groups of indicators instead of continuous variables. However, limitations of these baseline models include the inability to allow for arbitrary correlation in the errors for households in the same location and the fact that the linear probability model is likely misspecified because the predicted probabilities may be less than zero or larger than one for some observations.

To assess the sensitivity of our results, we used data for 2015 to estimate linear probability models that did not account for the survey features of the data but that accounted for unobserved features of households' locations to affect their financial choices and also allowed for arbitrary correlation in the errors for households in the same location. These models included income and the full set of other explanatory variables. Finally, we used data for 2015 to estimate probit models that did not account for the survey features of the data but that did account for the binary nature of the dependent variables. In this case, we model household location using region indicators only.

Caveats and Limitations

Our results have limitations and should be interpreted with caution. For example, our analysis does not establish a causal relationship between household characteristics and household behavior, only correlations. Our results may not generalize to other time periods. In addition, our results are indicative of household behavior on average, but the behavior of any one individual household may be different.

In some cases, our approach does not explain much of the variation in financial behaviors and characteristics of households. While we are able to explain 20 to 23 percent of the variation across households in the likelihood of having a checking or savings account, we are only able to

explain less than 5 percent of the variation across households in the likelihood of having a personal loan or line of credit from a bank in the past 12 months.

Furthermore, the data do not include variables identifying households' locations at levels of detail beyond the metropolitan area in which they live. Thus, we are not able to account for the influence of the characteristics of a household's local community that may influence their decisions, such as the numbers of banks and AFS providers nearby. However, recent research suggests that household socioeconomic and demographic characteristics generally play a larger role in determining household financial decisions—such as whether or not to open a bank account—than the characteristics of the community where the household lives.

Our estimates of the relationships between household behaviors and income may also reflect factors other than income. We controlled for several characteristics that may be associated with the household behaviors we analyzed and also may be correlated with income, such as race/ethnicity, educational attainment, and the homeownership rate. However, we may not have controlled for all possible characteristics that are associated with all household behaviors. If a characteristic we omitted from the analysis of some behavior is associated with income, then our results may reflect the relationship between that behavior and the omitted factor instead of, or in addition to, the relationship between household behavior and income.

Finally, our analysis of reasons why unbanked households are unbanked uses a relatively small number of observations. Only about 7 percent of households were unbanked in 2015, and our sample of unbanked households consists of 2,275 observations. The number of observations may not always be large enough to reveal significant differences in reasons for being unbanked for households with different incomes.

Results

Our estimates suggest that there are key differences in the use and accessibility of basic banking services for households with different incomes. In 2015, compared to otherwise similar households with $75,000 or more income, households with incomes of $29,999 or less were less likely to have a checking or savings account and more likely to have used general-purpose reloadable prepaid cards (see table 20). Lower-income households were more likely to use AFS providers for transactions and less likely to use only bank methods for paying bills and

receiving income than higher income households. Compared to otherwise similar households with $75,000 or more in income, households with lower incomes were less likely to use direct deposit.

Table 20: Estimated Differences in Methods for Obtaining Basic Banking Services for Lower-Income Households Relative to Households with Annual Income of $75,000 or More, 2015

	Estimated difference between the fraction of lower-income households and the fraction of similar households with annual income of $75,000 or more that:				
Household annual income	**had a checking or savings account**	**used alternative financial services providers for transactions in the past 12 months**	**used general-purpose reloadable prepaid cards in the past 12 months**	**typically received income and paid bills using methods associated with banks in past 12 months**	**used direct deposit**
Less than $15,000 (decimal points)	-0.151[a]	0.110[a]	0.044[a]	-0.213[a]	-0.232[a]
	(0.008)	(0.010)	(0.007)	(0.013)	(0.012)
$15,000 to $29,999 (decimal points)	-0.045[a]	0.074[a]	0.020[a]	-0.143[a]	-0.148[a]
	(0.005)	(0.008)	(0.006)	(0.010)	(0.009)
$30,000 to $49,999 (decimal points)	-0.000	0.044[a]	0.001	-0.082[a]	-0.079[a]
	(0.004)	(0.007)	(0.005)	(0.009)	(0.007)
$50,000 to $74,999 (decimal points)	0.011[a]	0.030[a]	0.007	-0.045[a]	-0.029[a]
	(0.003)	(0.006)	(0.006)	(0.008)	(0.006)
Sample size	36,189	36,189	36,189	31,304	34,275
R-squared	0.207	0.142	0.400	0.125	0.174

Source: GAO analysis of data from the Federal Deposit Insurance Corporation. | GAO-18-244

Notes: The table shows the estimated average difference between (1) the fraction of households with income in a given range using a basic banking service and (2) the fraction of similar households in the same metropolitan area or rural area with income of $75,000 or more using that service. These differences are estimated using linear probability regressions that also include controls for family type, tenure choice, and language spoken at home, as well as the age, education, labor force status, nativity and citizenship, and race/ethnicity of the head of the household, and location type and metropolitan area or rural area of state where the household is located. Standard errors calculated using successive difference replication based on the household weight and replicate weights are in parentheses.

[a]Statistically significant at the 1 percent level.

Our results for other years and other specifications were generally similar. Our estimates of the relationships between household income and the likelihoods that a household has a checking or saving account and used AFS providers for transactions are generally consistent with the findings of other research that analyzed household use of bank accounts and AFS providers for basic banking services.

Our estimates suggest that other characteristics of households are also associated with how households obtain basic banking services. For example, households that do not own their home are less likely than those that do to have a checking or saving account and more likely to use AFS providers for transactions. Households headed by an individual with more education are more likely to have a checking or savings account and less likely to use AFS providers for transactions. Households headed by someone who is unemployed or not in the labor force are less likely to have a checking or savings account than those headed by someone who is employed. Households headed by someone who is unemployed are more likely to use AFS providers for transactions than those headed by someone who is employed, while the opposite is the case for households headed by someone who is not in the labor force. The family type and the age, nativity and citizenship status, and race or ethnicity with which the head of household identifies are also associated with differences in households' methods for obtaining basic banking services.

Our estimates suggest that differences in income were associated with differences in the way households accessed basic banking services, even among households that had either a checking or savings account. In 2015, among households with checking or savings accounts, those with income from $15,000 to $74,999 were more likely to access their accounts via a bank teller than those with either higher or lower income, all else being equal (see table 21). In addition, compared to otherwise similar households with $75,000 or more in income, households with lower incomes were less likely to use ATMs or kiosks, telephone banking, online banking, and mobile banking. Contributing factors are that households with lower incomes were less likely than households with higher incomes to have home Internet access, mobile phones, and smartphones. Results for other years and other specifications were generally similar.

Table 21: Estimated Differences in Methods for Accessing Checking and Savings Accounts for Lower-Income Households Relative to Households with Annual Income of $75,000 or More, 2015

	Estimated difference between the fraction of lower-income households and the fraction of similar households with annual income of $75,000 or more that used:				
Household annual income	**bank teller**	**automated teller machine or kiosk**	**telephone banking**	**online banking**	**mobile banking**
Less than $15,000 (decimal points)	0.007	-0.125[a]	-0.055[a]	-0.236[a]	-0.127[a]
	(0.012)	(0.012)	(0.013)	(0.013)	(0.011)
$15,000 to $29,999 (decimal points)	0.048[a]	-0.093[a]	-0.048[a]	-0.201[a]	-0.125[a]
	(0.010)	(0.011)	(0.011)	(0.011)	(0.010)
$30,000 to $49,999 (decimal points)	0.039[a]	-0.055[a]	-0.035[a]	-0.143[a]	-0.095[a]
	(0.009)	(0.009)	(0.010)	(0.009)	(0.009)
$50,000 to $74,999 (decimal points)	0.029[a]	-0.031[a]	-0.019[b]	-0.067[a]	-0.053[a]
	(0.008)	(0.008)	(0.010)	(0.008)	(0.008)
Sample size	32,491	32,491	32,491	32,491	32,491
R-squared	0.050	0.126	0.050	0.268	0.203

Source: GAO analysis of data from the Federal Deposit Insurance Corporation. | GAO-18-244

Notes: The table shows the estimated average difference between (1) the fraction of households with income in a given range using a method for accessing checking and savings accounts and (2) the fraction of similar households in the same metropolitan area or rural area with income of $75,000 or more using the same method. These differences are estimated using linear probability regressions that also include controls for family type, tenure choice, and language spoken at home, as well as the age, education, labor force status, nativity and citizenship, and race/ethnicity of the head of the household, and location type and metropolitan area or rural area of state where the household is located. Standard errors calculated using successive difference replication based on the household weight and replicate weights are in parentheses.

[a]Statistically significant at the 1 percent level.

[b]Statistically significant at the 5 percent level.

Our estimates suggest that income differences are associated with some differences among unbanked households—households with neither a checking nor a savings account—in the reasons for being unbanked. In 2015, among unbanked households, those with lower incomes are just as likely as those with higher incomes to be unbanked because bank fees are too high or unpredictable, because banks do not offer needed products or services, because they do not trust banks, and because avoiding banks provides more privacy (see table 22). However, lower-income households—those with income of $49,999 or less—are more likely than higher-income households to be unbanked because they do not have enough money to keep in an account or because they have personal identification, credit, or former bank account problems. Finally, households with incomes from $30,000 to $74,999 are more likely than

other households to be unbanked because bank hours or locations are inconvenient.

Table 22: Estimated Differences in Reasons for Not Having Checking or Savings Accounts for Lower-Income Households Relative to Households with Annual Income of $75,000 or More, 2015

	Estimated difference between the fraction of lower-income households and the fraction of similar households with annual income of $75,000 or more that did not have a checking or savings account because:						
Household annual income	bank account fees are too high or unpredictable	banks do not offer needed products or services	they do not trust banks	avoiding banks provides more privacy	they do not have enough money to keep in an account	they have personal identification, credit, or former bank account problems	bank hours or locations are not convenient
Less than $15,000 (decimal points)	0.016	0.027	0.034	0.038	0.338[a]	0.092[a]	0.052
	(0.093)	(0.057)	(0.063)	(0.078)	(0.084)	(0.037)	(0.047)
$15,000 to $29,999 (decimal points)	0.009	0.060	0.061	0.077	0.266[a]	0.124[a]	0.024
	(0.092)	(0.059)	(0.062)	(0.079)	(0.082)	(0.041)	(0.044)
$30,000 to $49,999 (decimal points)	0.081	0.065	0.095	0.088	0.190[b]	0.071[c]	0.086[c]
	(0.097)	(0.061)	(0.067)	(0.083)	(0.086)	(0.042)	(0.050)
$50,000 to $74,999 (decimal points)	0.041	0.001	-0.017	0.058	0.034	0.072	0.125[b]
	(0.099)	(0.062)	(0.080)	(0.094)	(0.095)	(0.048)	(0.061)
Sample size	2,275	2,275	2,275	2,275	2,275	2,275	2,275
R-squared	0.179	0.152	0.180	0.199	0.223	0.174	0.150

Source: GAO analysis of data from the Federal Deposit Insurance Corporation. | GAO-18-244

Notes: The table shows the estimated average difference between (1) the fraction of households with income in a given range that cite a specific reason for not having a checking or savings account and (2) the fraction of similar households in the same metropolitan area or rural area with income of $75,000 or more that cite the same reason. These differences are estimated using linear probability regressions that also include controls for family type, tenure choice, and language spoken at home, as well as the age, education, labor force status, nativity and citizenship, and race/ethnicity of the head of the household, and location type and metropolitan area or rural area of state where the household is located. Standard errors calculated using successive difference replication based on the household weight and replicate weights are in parentheses.

[a]Statistically significant at the 1 percent level.

[b]Statistically significant at the 5 percent level.

[c]Statistically significant at the 10 percent level.

Results for other specifications for 2015 were generally similar. Results for other years were also generally similar, but with some exceptions. In 2013, households with income of $74,999 or less were no more likely than households with income of $75,000 or more to report being unbanked because they did not have enough money to keep in an account. Households with income of $29,999 or less or from $50,000 to $74,999 were no more likely than households with income of $75,000 or more to report being unbanked because they had identification, credit, or former bank account problems. Finally, households with income from $30,000 to $74,999 were not more likely than households with income of $75,000 or more to report being unbanked because bank hours or locations were inconvenient.

Our estimates suggest that income differences are associated with differences in households' desire for small-dollar, unsecured loans and where they obtain this type of credit. Households with lower incomes are less likely to have saved for unexpected expenses or emergencies and more likely to have fallen behind on bills in the past 12 months than households with higher incomes, suggesting that their demand for small-dollar, unsecured loans may be higher (see table 23). However, households with lower incomes were more likely to have obtained credit from an AFS provider and less likely to have used a credit card in the past 12 months than similar households with higher incomes.

Table 23: Estimated Differences in Savings, Bill Paying, and Consumer Credit Behaviors for Lower-Income Households Relative to Households with Annual Income of $75,000 or More, 2015

	Estimated difference between the fraction of lower-income households and the fraction of similar households with annual income of $75,000 or more that:						
Household annual income	**set aside money for unexpected expenses or emergencies**	**fell behind on bills**	**used alternative financial services providers for credit**	**used credit cards**	**had consumer credit from a bank**	**desired consumer credit[a]**	**were consumer credit constrained[b]**
Less than $15,000 (decimal points)	-0.274[c]	0.185[c]	0.039[c]	-0.332[c]	-0.059[c]	-0.050[c]	0.031[c]
	(0.012)	(0.009)	(0.007)	(0.012)	(0.008)	(0.010)	(0.006)
$15,000 to $29,999 (decimal points)	-0.191[c]	0.140[c]	0.035[c]	-0.202[c]	-0.045[c]	-0.030[c]	0.037[c]
	(0.010)	(0.009)	(0.006)	(0.009)	(0.008)	(0.008)	(0.007)
$30,000 to $49,999 (decimal points)	-0.120[c]	0.086[c]	0.036[c]	-0.108[c]	-0.032[c]	-0.037[c]	0.020[c]
	(0.010)	(0.007)	(0.005)	(0.009)	(0.007)	(0.008)	(0.005)
$50,000 to $74,999 (decimal points)	-0.060[c]	0.049[c]	0.015[c]	-0.047[c]	-0.021[c]	-0.016[d]	0.016[c]
	(0.008)	(0.006)	(0.004)	(0.007)	(0.007)	(0.008)	(0.005)
Sample size	33,531	36,189	36,189	33,759	33,743	36,189	36,189
R-squared	0.160	0.127	0.065	0.283	0.043	0.046	0.047

Source: GAO analysis of data from the Federal Deposit Insurance Corporation. | GAO-18-244

Notes: The table shows the estimated average difference between (1) the fraction of households with income in a given range exhibiting a behavior and (2) the fraction of similar households in the same metropolitan area or rural area with income of $75,000 or more exhibiting the same behavior. These differences are estimated using linear probability regressions that also include controls for family type, tenure choice, and language spoken at home, as well as the age, education, labor force status, nativity and citizenship, and race/ethnicity of the head of the household, and location type and metropolitan area or rural area of state where the household is located. Standard errors calculated using successive difference replication based on the household weight and replicate weights are in parentheses.

[a]A household desired consumer credit if it applied for a new credit card or personal loan or line of credit at a bank (excluding student loans or loans taken out for major purchases like a house or car), or wanted to but did not for fear of being turned down.

[b]A household was credit constrained if it applied for a new credit card or personal loan or line of credit from a bank and was partially or fully turned down, or wanted a new credit card or a personal loan or line of credit from a bank but did not apply for fear of being turned down.

[c]Statistically significant at the 1 percent level.

[d]Statistically significant at the 5 percent level.

Furthermore, households with lower incomes were less likely to have had a personal loan or line of credit from a bank in the past 12 months (excluding student loans or loans taken out for major purchases like a house or car) than households with higher incomes. They were both less likely to have desired this type of credit from a bank and more likely to have found themselves unable to access this type of credit from a bank, even though they were willing to pay the going interest rates. Altogether, these results suggest that lower-income households are likely to have greater demand for small-dollar unsecured loans than higher-income households, but are less likely to obtain them from traditional banks and more likely to obtain them from AFS providers. Results for other years and other specifications were generally similar.

Our estimates also suggest that other characteristics of households are also associated with factors that affect demand for small-dollar, unsecured loans. For example, households that do not own their home are less likely than those that do to save for emergencies, to have a credit card, or to have a consumer loan from a bank. They are more likely to fall behind on bills and to obtain credit from an AFS provider. Households headed by an individual with more education are more likely to have emergency savings and credit cards and less likely to fall behind on bills or obtain credit from an AFS provider. Households headed by someone who is unemployed or not in the labor force are less likely than those headed by someone who is employed to have emergency savings or a credit card. Those headed by someone who is unemployed are more likely to obtain credit from an AFS provider, while those who are not in the labor force are not. Finally, we also controlled for family type, age, nativity and citizenship status, and the race or ethnicity with which the head of household identifies, and we found that these factors were sometimes significant.

Additional Information on the National Survey of Unbanked and Underbanked Households

The National Survey of Unbanked and Underbanked Households data used in this analysis were collected through supplements to the Current Population Survey (CPS). The CPS is the primary source of information on the labor force characteristics of the U.S. population, including employment, unemployment, and earnings statistics. It also includes a variety of demographic characteristics, such as age, sex, race, marital status, and educational attainment. The CPS sample consists of independent samples in each state and the District of Columbia. The sample sizes for each state are set so that specific precision requirements for estimating unemployment rates will be met. The sample design ensures that most of the households in a given state have the

same probability of being selected, though, in general, household selection probabilities will vary across states. Because the CPS design is state-based, most of the estimates for the National Survey of Unbanked and Underbanked Households should be precise at the state level and for some metropolitan statistical areas.

For the June 2015 CPS, a statistical sample of 60,841 survey-eligible households was selected from the sampling frame. Of these households, 52,801 participated in the CPS, resulting in an 87 percent response rate. There were 8,040 nonrespondent eligible households. Most of these nonrespondents either refused to participate (66 percent) or were not home at the time of the interview visit or call (20 percent). The remaining 14 percent consisted of households where (1) the household respondent was temporarily absent, (2) the household could not be located, (3) language barriers prevented the interview, or (4) other reasons. Because of the availability of translators for many languages, only 0.5 percent of the nonrespondents (37 households) did not participate as a result of language barriers. Sample sizes and response rates for the June 2011 and June 2013 CPS were similar.

Coverage ratios for the CPS are derived as a measure of the percentage of persons in the target universe—the U.S. civilian, noninstitutionalized population, aged 15 or older—that are included in the sampling frame. The overall coverage ratio for the June 2015 CPS was 89 percent. The missing 11 percent consists of three groups: (1) persons residing in households that are not in the CPS sampling frame, (2) noninstitutionalized persons not residing in households at the time the CPS was conducted, and (3) household residents that were not listed as household members for the CPS for various reasons. The overall coverage ratios for the June 2011 and June 2013 CPS were similar.

All households that participated in the June 2011, 2013, and 2015 CPS were eligible to participate in the National Survey of Unbanked and Underbanked Households. However, only households whose respondents specified that they had some level of participation in their household finances and responded “Yes” or “No” to whether someone in their household had a bank account were considered survey respondents. All other CPS household respondents were asked no further questions and were classified as nonrespondents for the supplement. Of the 52,801 households that participated in the CPS in June 2015, 36,189 (69 percent) also participated in the National Survey of Unbanked and Underbanked Households. For the June 2011 and June 2013 CPS, 84 percent and 77 percent of participating households, respectively, also

participated in the National Survey of Unbanked and Underbanked Households. The weights calculated by the Census Bureau for the CPS and the National Survey of Unbanked and Underbanked Households respondents were adjusted to account for both nonresponse and undercoverage. These weight adjustments help correct any biases in estimates because of nonresponse and undercoverage, so that results from the CPS are representative of the U.S. civilian, noninstitutionalized population, aged 15 or older.

Appendix IV: Additional Information on Options That Could Further Encourage Banking Services and Small-Dollar Loans

Our work identified a number of suggested options not related to the Community Reinvestment Act (CRA) that could further encourage financial institutions to provide basic banking services and small-dollar, nonmortgage consumer loans in low- and moderate-income (LMI) areas.[1] We drew information from all the methodological approaches we conducted to include in this thematically organized and comprehensive appendix, including a literature review, interviews, affinity mapping exercise, stakeholder survey, and discussion groups.[2] This appendix provides additional information on suggested options in the following two areas: (1) changes designed to address concerns among financial institutions about the profitability and safety and soundness of such loans and (2) changes in other non-CRA areas. While our analysis did not allow us to form conclusions on the merits of the suggested options, we present the strengths and weaknesses of them as identified by stakeholders.

Suggested Options That Address Concerns about Profitability and Safety and Soundness

According to knowledgeable stakeholders, suggested options designed to address concerns about profitability and safety and soundness could further encourage financial institutions to provide small-dollar, nonmortgage consumer loans in LMI areas.[3] Such options could include lessening underwriting restrictions on loans under a certain dollar amount and clarifying interest rate maximums. Several participants in our think tank discussion group noted that these types of options would be the most important ones to encourage more small-dollar loans within the marketplace. Two participants in our industry discussion group stated that regulatory restrictions, both implicit and explicit, have made it difficult for banks to provide accessible and affordable small-dollar, nonmortgage

[1]Congress passed CRA in 1977 to encourage banking institutions to meet the credit needs of the communities in which they operate, including LMI communities, consistent with safe and sound banking operations. Basic banking services refers to those financial services needed to allow the average consumer to engage in necessary day-to-day banking activities. These services include deposit taking and simple transaction or savings account programs with low fees. While there is no single definition of small-dollar, nonmortgage consumer loans, the term generally refers to unsecured, nonmortgage consumer loans that are less than $2,500. These products may include various fees, interest rates, and terms.

[2]During the affinity mapping exercise, we grouped the options we identified from both the literature review and interviews into a consolidated set of suggested options.

[3]This section does not discuss basic banking services, as stakeholder concerns were primarily focused on small-dollar lending. However, some stakeholders noted that due to the typically low-dollar balances in accounts maintained by LMI individuals, financial institutions have concerns about the profitability of basic banking services as well.

consumer loans. However, the Consumer Financial Protection Bureau (CFPB) recently published a final rule that may affect banks' willingness to make small-dollar, nonmortgage consumer loans.[4]

In the literature we reviewed and interviews, stakeholders suggested options that regulators could adopt that would address concerns about profitability and safety and soundness.[5] Suggested options include:

- **Establishing low-cost, streamlined underwriting requirements.** For example, an article by a representative of the Pew Charitable Trusts described how low-cost, streamlined underwriting requirements that require little documentation would allow banks to make small-dollar, nonmortgage loans profitably.[6] A former Federal Deposit Insurance Corporation (FDIC) chair agreed, telling us that for loans under a certain amount, regulators should require less underwriting

[4]On November 17, 2017, CFPB issued a final rule that, among other things, governs the underwriting of certain personal loans with short-term or balloon payment structures. See "Payday, Vehicle Title, and Certain High-Cost Installment Loan Rule," 82 Fed. Reg. 54472 (Nov. 17, 2017). According to CFPB, the rule is "aimed at stopping payday debt traps by requiring upfront whether consumers have the ability to repay their loans." Under the new rule, lenders that make short-term loans of 45 days or less or longer-term balloon payment loans generally must make an "ability-to-repay" determination, that is, must reasonably determine that the consumer will be able to make payments on the loan while also meeting major financial obligations and basic living expenses. (Loans made by a lender who makes 2,500 or fewer covered loans per year and derives no more than 10 percent of its revenue from such loans are exempt from the CFPB rule. According to CFPB, these are usually small personal loans made by community banks or credit unions to existing customers or members.) The rule also covers a third type of loan—loans with a term longer than 45 days with an annual percentage rate (APR) over 36 percent that gives the lender account access. These loans are not subject to the ability-to-repay provisions but are subject to certain penalty fee prevention provisions. According to CFPB, these protections give consumers a chance to dispute any unauthorized or erroneous attempts by a lender to collect payment from the borrower's account and to arrange for unanticipated payments that are due. Since the compliance date for most provisions of the rule, including these provisions, is August 2019, its impact on banks' willingness to make small-dollar, nonmortgage consumer loans is not currently clear. CFPB recently released a statement that it intended to engage in a rulemaking process that reconsidered the payday rule.

[5]Financial institutions are subject to safety and soundness examinations. These examinations generally assess a bank's soundness, determine the level of risk involved in the bank's transactions and activities, and ascertain the extent of compliance with banking laws and regulations.

[6]N. Bourke, "Regulators Should Let Banks Get Back to Small-Dollar Loans," September 16, 2015, accessed on July 31, 2017, https://www.americanbanker.com/opinion/regulators-should-let-banks-get-back-to-small-dollar-loans.

and allow income evaluations for small loans that are less burdensome than those for larger loans. FDIC conducted a small-dollar loan pilot program that resulted in a template for small-dollar loans that included a streamlined underwriting system enabling banks to issue a loan decision within 24 hours of a loan application.[7]

One participant in our industry discussion group stated that streamlining underwriting requirements would help banks automate underwriting processes and lower costs. However, several participants in our advocacy discussion group did not support streamlining underwriting requirements because it could be considered deregulation. Several participants added that regulation is necessary to ensure safe and sound lending and therefore long-term benefits for everyone.

One participant in our nonfederal banking regulator discussion group suggested using alternative data sources for underwriting because there are individuals who do not have a traditional credit history. For example, this participant noted that using utility and phone bill payment history, or a referral system where one person vouches for the credit worthiness of another, have worked in some instances. However, another participant cautioned that using alternative data could lead to fair lending concerns, depending on which variables were used to determine access to credit. Another participant elaborated, stating that using alternative data to make credit underwriting decisions could be a concern if the variables used are correlated with race, national origin, or any other prohibited areas.

One federal banking regulator expressed concern that easing underwriting regulations could be perceived as undermining safety and soundness. Further, one Office of the Comptroller of the Currency (OCC) official noted that the agency had already sought comments from the public on issuing a special-purpose charter for non-deposit taking institutions to allow them to offer products that use online underwriting techniques to expand the type of borrowers who could

[7]FDIC conducted a small-dollar loan pilot program from 2007 through 2009 designed to illustrate how banks can profitably offer affordable small-dollar loans as an alternative to high-cost credit products such as payday loans and fee-based overdraft programs. The pilot program resulted in a template for small-dollar loans: low or no-fee loans of $2,500 or less, with a term of 90 days or more, an APR of 36 percent or less, and a streamlined underwriting system enabling banks to issue a loan decision within 24 hours of a loan application.

qualify for certain products.[8] One participant in our federal banking regulator discussion group stated that offering a non-depository charter could make loan markets more efficient and broaden them to allow for servicing of nontraditional consumers.

- **Allowing higher interest rates.** One industry representative noted that loans to LMI borrowers tend to be less profitable and riskier than others, so a higher interest rate is warranted. Several stakeholders suggested allowing banks to charge an interest rate above the 36 percent perceived cap on small-dollar loans.[9] For example, one article stated that easing the 36 percent APR upper limit (cap) may prompt more banks to provide small-dollar loans to higher-risk consumers that rely on products from alternative financial services providers.[10] According to representatives from a think tank we interviewed, banks have told them that the small-dollar loans currently receiving CRA credit are not profitable and therefore not viable because of the low interest rates (below 36 percent APR) they would have to charge. For example, the think tank representatives observed that a small-dollar loan with an effective APR of 75 percent would still be far less costly to borrowers than many payday loans and would have smaller fees.

  One participant in our industry discussion group believed regulators would view a small-dollar loan with a high interest rate for LMI borrowers unfavorably. Another participant stated that even if regulators made such a change, it may not result in increased offerings of small-dollar loan products. Additionally, a report from a consumer advocacy organization argued that an interest rate cap at 36 percent would incentivize lenders to offer loans with longer term

[8]OCC's special-purpose charter would allow OCC to grant a special-purpose national bank charter to a financial technology, or "fintech," company. Fintech subsectors such as marketplace lending and mobile payments may provide consumers with additional options for accessing credit and banking services. For more information, see *GAO, Financial Technology: Information on Subsectors and Regulatory Oversight*, GAO-17-361 (Washington, D.C.: Apr. 19, 2017).

[9]CFPB's new rule subjects to certain penalty fee provisions longer-term loans with interest rates above 36 percent that give the lender account access. The implication this has for banks' willingness to make small-dollar loans is not yet known.

[10]S. M. McKernan, C. Ratcliffe, and D. Kuehn, "Prohibitions, price caps, and disclosures: A look at state policies and alternative financial product use," *Journal of Economic Behavior & Organization*, vol. 95 (2013). Alternative financial services providers include transaction providers such as check cashing outlets and money transmitters and credit providers such as payday loan stores, automobile title lenders, and pawnshop lenders.

structures and avoid making loans that borrowers cannot repay.[11] Several participants in our advocacy discussion group did not support allowing higher interest rates because it could be construed as deregulation.

Federal banking regulator officials said that they considered interest rates for individual products on a case-by-case basis, and did not discount the possibility of giving CRA consideration for loans with interest rates above 36 percent. However, during its small-dollar loan pilot program from 2007 through 2009, FDIC anticipated most programs would be consistent with its Affordable Small-Dollar Loan Guidelines that required interest rates no greater than 36 percent, although participating financial institutions had some flexibility to encourage innovation.[12] This pilot was designed to illustrate how financial institutions can profitably offer affordable small-dollar loans as an alternative to high-cost credit products such as payday loans and fee-based overdraft programs.[13]

- **Minimizing compliance risk.** Stakeholders explained how minimizing compliance risk—risk arising from violations of, or nonconformance with, laws, rules, and regulations—would allow banks to offer profitable and safe small-dollar loans. For example, representatives from a think tank stated that financial institutions would not make small-dollar loans if they have to be fully underwritten, citing exposure to compliance risk. Additionally, FDIC's 2011 survey of financial institutions' efforts to serve the unbanked and underbanked found that 35 percent of institutions cited regulatory requirements as a major obstacle in serving unbanked and underbanked consumers and an additional 30 percent cited them as a minor obstacle; 35 percent of

[11]National Consumer Law Center, *Why 36%? The History, Use, and Purpose of the 36% Interest Rate Cap* (Washington, D.C.: April 2013).

[12]See Federal Deposit Insurance Corporation, "A Template for Success: The FDIC's Small-Dollar Loan Pilot Program," *FDIC Quarterly*, vol. 4, no. 2 (2010). The pilot's definition of small-dollar loans was consistent with small-dollar loan guidelines that FDIC had issued in 2007. See Federal Deposit Insurance Corporation, "Affordable Small-Dollar Loan Products: Final Guidelines," Financial Institution Letter (FIL)-50-2007 (Washington, D.C.: June 19, 2007).

[13]The pilot defined small-dollar loans as low or no-fee loans of $2,500 or less, with a term of 90 days or more, an APR of 36 percent or less, and a streamlined underwriting system enabling financial institutions to issue a loan decision within 24 hours of a loan application. In general, the new CFPB rule imposes "ability-to-repay" requirements on loans with a duration of 45 days or less or longer-term loans with a balloon payment.

these institutions reported fair lending/compliance as a major obstacle in offering financial products and services to underserved consumers.[14]

One participant in our think tank discussion group discussed how giving financial institutions more flexibility in determining how best to meet the needs of their customers, as opposed to having regulators be more prescriptive via regulation, would help avoid some of the heavy costs that can come with additional financial regulations. Another participant discussed how safety and soundness examiners and CRA examiners may have differing views on the safety of such loans, so it would be important to ensure consistency within the federal banking regulators to mitigate these concerns.

Several stakeholders discussed the idea of allowing banks to innovate in a safe and sound manner. For example, one participant in our think tank discussion group stated that compliance risk could be minimized by ensuring banks were protected under “safe harbor” rules that allowed them to experiment with different products and delivery methods without repercussions from regulators as long as they adhere to the regulatory guidelines. However, one participant in our advocacy discussion group noted that guidance from regulators about the level of innovation appropriate at a particular financial institution often lacks safe harbor language. Further, a participant in our think tank discussion group noted that CFPB staff do not always want to issue no-action letters.[15]

[14]Federal Deposit Insurance Corporation, “2011 FDIC Survey of Banks’ Efforts to Serve the Unbanked and Underbanked” (Washington, D.C.: December 2012).

[15]CFPB staff, at their discretion, can issue no-action letters to specific applicants in instances involving innovative financial products or services that promise substantial consumer benefit where there is substantial uncertainty whether or how specific provisions of statutes implemented or regulations issued by the Bureau would be applied (for example if, because of intervening technological developments, the application of statutes and regulations to a new product is novel and complicated).

Other Suggested Options Unrelated to CRA That Address Serving LMI Consumers

According to knowledgeable stakeholders, additional options not related to CRA could further encourage financial institutions to provide basic banking services and small-dollar, nonmortgage consumer loans in LMI areas. Such options include encouraging partnerships that promote basic banking services and small-dollar, nonmortgage consumer loans and sharing leading practices.

Encouraging Financial Institutions to Take Advantage of Existing Options

In the literature we reviewed and interviews, stakeholders suggested ways that financial institutions could take advantage of existing options to increase the number of basic banking services and small-dollar, nonmortgage consumer loans. Existing options include:

- **Creating loan pool consortiums or guarantees.** One stakeholder suggested loan pool consortiums as one way institutions could reduce overhead costs and help share risk.[16] Further, representatives of an advocacy organization suggested creating a loan pool consortium that provides small-dollar loans on a large volume to reduce overhead costs to individual banks and share the credit risks. Further, in its assessment of its small-dollar loan pilot program, FDIC noted that the creation of pools of non-profit or government operating funds to serve as "guarantees" for safe small-dollar loan programs could increase the availability and accessibility of such products.[17] The assessment stated that several existing small-dollar loan programs feature guarantees in the form of loan loss reserves or linked, low-cost deposits provided by government bodies or philanthropic groups. FDIC's report also noted these guarantees provide important assurances to financial institutions that are interested in offering small-dollar loans but are concerned about the costs of doing so.
- **Focusing on relationship banking.** Several stakeholders stated that banks should consider making small-dollar, nonmortgage consumer loans to develop long-term relationships with borrowers. For example, the Center for Financial Services Innovation has written that lenders should prioritize long-term relationships that small-dollar loans can

[16]A loan consortium is formed by the joining of two or more financial institutions to invest in a pool of funds and make loans to a borrower using participation loans or lines of credit. Investors in a loan consortium share the costs and risks of lending. Each investor allows a prorated draw based on its respective commitment amount and shares any losses proportionally.

[17]Federal Deposit Insurance Corporation, "A Template for Success: The FDIC's Small-Dollar Loan Pilot Program."

generate over short-term profits that may not be attainable.[18] It noted that while creating small-dollar loans that are both affordable and profitable can be challenging, developing such products will allow lenders to establish and strengthen relationships with new and existing customers who may return for additional products and services over time. Additionally, bankers who participated in FDIC's small-dollar loan pilot program indicated that they primarily used small-dollar loans to build or retain profitable, long-term relationships with consumers.[19]

Several of our discussion group participants supported the idea of relationship banking. One participant in our industry discussion group mentioned that one successful model is the character loan—a good faith (unsecured) loan based on the borrower's financial position, reputation in the community, and his or her payment history with the same or other bank(s). This participant noted character lending is a worthwhile model because the bank can get credit within the community for offering such loan products. A participant in our nonfederal banking regulator discussion group explained that the National Credit Union Administration's (NCUA) payday-alternative loan is popular and successful in achieving its goal of helping build credit and move people into a traditional financial institution who previously were not a part of mainstream finance or in an existing banking relationship.[20] If a short-term, small amount loan borrower has no prior relationship with the credit union, there is a greater risk that the borrower may walk off with unsecured cash and never return. However, under the payday-alternative loan program, NCUA has found that if the borrower is a member of the credit union for a minimum of one month before receiving a short-term small loan, this will reduce the chance of default.

- **Offering lower-risk accounts.** In a letter to the 25 largest retail banks in the U.S., CFPB encouraged these banks to provide lower-

[18]Center for Financial Services Innovation, "Designing High-Quality, Small-Dollar Credit: Insights from CFSI's Test & Learn Working Group" (Chicago, IL: 2015).

[19]Federal Deposit Insurance Corporation, "A Template for Success: The FDIC's Small-Dollar Loan Pilot Program."

[20]NCUA regulations permit federally-chartered credit unions to make payday-alternative loans. Payday-alternative loans have a mandated interest rate cap that is 1000 basis points above the maximum interest rate cap established by the NCUA Board for all other federal credit union loans. The payday-alternative loan interest rate cap is currently 28 percent.

risk accounts to all consumers, including underserved populations. Specifically, CFPB encouraged these banks to offer products that are designed not to authorize overdrafts and that do not charge overdraft fees. CFPB took this step due to concerns that consumers were being sidelined by the lack of account options. Although a number of institutions had introduced “no-overdraft” accounts and offered them alongside more common checking account products, it found in a review of the top retail banking websites that nearly half did not appear to offer any deposit account that ensures consumers cannot overspend. It concluded that such a product would give consumers an opportunity to choose an account that helps them avoid overdrafting.

- **Implementing technological solutions.** Stakeholders suggested that lenders adopt technological solutions such as software platforms that enable the lender to process applications for financial products more efficiently, thereby reducing costs and increasing speed. For example, the Center for Financial Services Innovation noted in a paper on designing high-quality, small-dollar credit that profit margins of small-dollar loans are relatively low, so lenders must find ways to responsibly reduce cost.[21] It also stated that adopting technology solutions and streamlining the application process would allow providers to do this, while yielding faster processing times for borrowers. A former FDIC chair agreed and told us that financial institutions should be allowed to use technology to determine loan repayability. FDIC’s report on its small-dollar loan pilot program suggested further study on such technologies.[22]
- **Increasing marketing.** Stakeholders described how additional marketing could be used to increase the number of small-dollar loans and basic banking services. The Center for Financial Services Innovation noted that lenders should use creative marketing to achieve critical mass in new customers.[23] They explained in addition to reducing operational costs through automation, lending at high volumes can be fundamental to covering costs and maintaining profits over time. The Center for Financial Services Innovation further described how pursuing innovative marketing strategies—such as

[21]Center for Financial Services Innovation, “Designing High-Quality, Small-Dollar Credit: Insights from CFSI’s Test & Learn Working Group.”

[22]Federal Deposit Insurance Corporation, “A Template for Success: The FDIC’s Small-Dollar Loan Pilot Program.”

[23]Center for Financial Services Innovation, “Designing High-Quality, Small-Dollar Credit: Insights from CFSI’s Test & Learn Working Group.”

targeted messaging campaigns and partnerships with community organizations—can help institutions attract new customers. Additionally, CFPB noted in its letter to the top 25 retail banks on lower-risk checking accounts that the lack of marketing for these products, in particular, had lessened their visibility and lowered their use among consumers who might otherwise benefit from their availability. Thus, the agency urged institutions that already offered such accounts to feature them among their standard account offerings both in their branches and online. However, one participant in our industry discussion group explained that one problem with creative marketing is that it is expensive and thus would cut into the profitability of small-dollar loans. Instead, institutions have relied on cheaper word of mouth advertising or marketing within branches.

As noted previously, some stakeholders stated that while changes to CRA could help encourage financial institutions to provide more basic banking services and small-dollar loans, they may not be enough to overcome bigger concerns about profitability and safety and soundness. Some stakeholders said the same about taking advantage of existing options. For example, one participant in our think tank discussion group noted that there are a lot of existing options for small-dollar loans, but banks have concerns about profitability and negative repercussions from their prudential regulators. Similarly, a participant in our nonfederal banking regulator discussion group had heard from individuals at community banks and credit unions that although certain financial institutions such as credit unions and community banks are making small-dollar loans on a small scale to assist their customers, they are not doing so on a large scale because such loans do not generate a profit.

FDIC has issued guidance to inform institutions of risks related to deposit advance products.[24] In that guidance, FDIC noted that a number of financial institutions were currently offering reasonably priced small-dollar loans at reasonable terms to their customers and

[24]A deposit advance product is a small-dollar, short-term loan or line of credit that a bank makes available to a customer whose deposit account reflects recurring direct deposits. The customer obtains a loan, which is to be repaid from the proceeds of the next direct deposit. These loans typically have high fees, are repaid in a lump sum in advance of the customer's other bills, and often are not subject to fundamental and prudent banking practices through which a bank can determine the customer's ability to repay the loan and meet other necessary financial obligations. FDIC and OCC issued guidance on the use of deposit advance products. OCC rescinded it upon the release of the new CFPB regulations, but the FDIC guidance remains in effect.

encouraged institutions to develop new or innovative programs to meet the need for small-dollar credit in a safe and sound manner.

Encouraging Partnerships That Promote Basic Banking Services and Small-Dollar Loans

In the literature we reviewed and interviews, stakeholders suggested that regulators could encourage financial institutions to enter into partnerships with other entities that promote accessible and affordable basic banking services and small-dollar, nonmortgage consumer loans. Suggested options include:

- **Encouraging partnerships between financial institutions and community groups.** Stakeholders noted that partnerships between financial institutions and community groups can help promote checking and savings account ownership and small-dollar loans. In an FDIC survey, community outreach collaborations were identified as the most effective strategy for developing relationships with underserved populations.[25] Additionally, pilot bankers participating in FDIC's small-dollar loan pilot program reported that partnerships with community groups were crucial to the success of their programs.[26] Among other things, the bankers noted that these partnerships can serve as an incentive to banks by providing client referrals and the opportunity for other parties to share in program costs. In addition, one participant in our think tank discussion group stated that partnerships with community organizations might be a useful way to promote banks that have no-overdraft accounts and thus help bring people back into the banking system.

  One participant in our advocacy discussion group pointed to FDIC's safe account pilot as an example of a good partnership.[27] Under the pilot, participating financial institutions partnered with nonprofit organizations, community groups, businesses, and local or state government agencies and officials to conduct outreach and market

[25]Federal Deposit Insurance Corporation, "2011 FDIC Survey of Banks' Efforts to Serve the Unbanked and Underbanked." FDIC asked institutions to identify the most effective marketing channel. Among all banks surveyed, 38.5 percent selected community outreach collaborations. Other options included newspapers, brochures, or other print advertising; direct mail; billboard advertising/signage outside of branches; and TV or radio advertising.

[26]Federal Deposit Insurance Corporation, "A Template for Success: The FDIC's Small-Dollar Loan Pilot Program."

[27]On January 1, 2011, FDIC launched a 1-year pilot program, the Model Safe Accounts Pilot, with nine financial institutions to determine the feasibility of offering safe, low-cost transaction and basic savings accounts (safe accounts) to help meet the needs of underserved and LMI consumers.

safe accounts to underserved consumers. In its final report on the pilot, FDIC noted that pilot institutions found partnerships to be particularly useful in reaching the targeted unbanked and underbanked consumers.[28]

However, multiple participants in our industry discussion group noted that banks that partner with nonprofit organizations have sometimes been unable to maintain the volume of business necessary to make small-dollar loans profitable.

- **Encouraging partnerships between banks and credit unions.** Encouraging partnerships between banks and credit unions was suggested by one stakeholder as a way to encourage financial institutions to increase access to basic banking services and small-dollar, nonmortgage consumer loans. Officials from an industry group representing credit unions described how the cost of providing basic banking services and small-dollar lending is a challenge for financial institutions because there are overhead and operating costs associated with these services. They noted that this challenge may be overcome through partnerships between banks and credit unions. As an example, they cited a product called Borrow and Save, which provides borrowers with access to small-dollar credit opportunities that are affordable and cost less than alternative loan options and help borrowers strengthen their financial condition with a required savings component.

  Additionally, a participant in our nonfederal banking regulator discussion group agreed that bank-credit union partnerships could be useful, noting that credit unions do not operate under the same regulatory constraints banks do and can thus reach populations or offer products that might not be possible for banks.

- **Encouraging partnerships between financial institutions and community development financial institutions (CDFI).** Several stakeholders suggested partnerships with CDFIs as a way to increase small-dollar loans.[29] Specifically, a U.S. Treasury Department white paper suggested that online marketplace lenders should partner with

[28]Federal Deposit Insurance Corporation, *FDIC Model Safe Accounts Pilot: Final Report* (Washington, D.C.: April 2012).

[29]CDFIs expand economic opportunity in low-income communities by providing access to financial products and services for local residents and businesses. They can be banks, credit unions, loan funds, microloan funds, or venture capital providers.

CDFIs to offer loans to LMI communities.[30] The white paper noted that through partnerships, CDFIs may be able to utilize online marketplace lenders' underwriting technology and back-end operations to increase efficiencies and lower costs. Further, the white paper theorized that online marketplace lenders could, in turn, tap into the local knowledge and understanding of credit markets of CDFIs to reach more borrowers in distressed communities.

A participant in our industry discussion group discussed how partnerships could help larger banks serve communities they might otherwise be unable to reach. In particular, the participant noted that CDFIs have emerged as a method of extending reach and offloading cost and risk to make the banking system work better for the customer. One participant in our nonfederal banking regulator discussion group noted that the CDFI Fund is an example of a successful partnership model that helps provide products and services in LMI communities.[31] However, a participant in our industry discussion group explained that while CDFIs extend reach and offload risk, they have limited capacity so they must be careful not to overextend themselves.

Participants in our advocacy discussion group noted that encouraging partnerships between financial institutions and other entities might have unintended results. For example, one participant noted that banks often partner with payday lenders and tax providers to make refund anticipation loans that may be abusive. Another stated that while there are many responsible fintech companies, some fintech companies bring abusive financial products and practices to market. In addition, one participant in our nonfederal banking regulator discussion group noted safety and soundness examiners sometimes do not understand financial institution partnerships with CDFIs. While a financial institution may enter into such a partnership to deliver products and services that help them receive CRA credit, the institution's safety and soundness examiner may not understand how the relationship fits into the institution's business model. Another participant explained that regulators might disagree with the idea

[30]U.S. Department of the Treasury, "Opportunities and Challenges in Online Marketplace Lending" (Washington, D.C.: May 20, 2016). Marketplace lenders connect consumers and small businesses seeking online and timelier access to credit with individuals and institutions seeking profitable lending opportunities.

[31]Through financial and technical assistance, the CDFI Fund supports CDFIs.

of encouraging partnerships with marketplace lenders because such lending is not a proven business model.

Two federal banking regulator officials mentioned that their agency is already encouraging partnerships, through publications describing best practices around partnerships, issuance of guidelines, advisory committees, and convening coalitions of bankers, community organizations, and agencies. Additionally, partnerships are already considered under CRA, particularly for large institutions under the investment test and intermediate small institutions under the community development test. For example, financial institutions may receive credit on the investment test for investments, loan participations, and other ventures undertaken in cooperation with minority- or women-owned financial institutions and low-income credit unions. Additionally, institutions can receive CRA credit for partnerships with nonprofit organizations that offer financial counseling or other community development services to LMI communities.

Sharing Leading Practices to Encourage Basic Banking Services and Small-Dollar Loans

In the literature we reviewed, interviews, and discussion groups, stakeholders suggested that regulators could share leading practices to encourage banks to provide more basic banking services and small-dollar, nonmortgage consumer loans. For example, in comments on recent proposed changes to the *Interagency Questions and Answers Regarding Community Investment* (CRA Q&A), one advocacy organization stated that federal banking regulators should create a clearinghouse for CRA-related innovations.[32] A participant in our advocacy discussion group noted that by highlighting programs and innovations, regulators would be providing a backdoor safe harbor that would alleviate bank sensitivities to regulatory, reputational, and financial loss risks. Another participant stated that sharing information about

[32]The CRA Q&As provide guidance on CRA examinations to financial institutions and the public. They were updated in July 2016. 81 Fed. Reg. 48506 (July 25, 2016).

successful programs like the North Carolina credit union program that are profitable and sustainable would be helpful.[33]

One participant in the advocacy discussion group stated that information sharing does not always lead to improved results. The participant cited FDIC's small-dollar loan pilot as an example, stating that the agency shared the results of the pilot with its member banks but this did not result in many new small-dollar loan products being offered. Another participant noted that some practices are not replicable on a large scale.

The federal banking regulators have recognized the value of leading practices and shared some. In its assessment of its small-dollar loan pilot program, FDIC suggested that one way to encourage more financial institutions to offer small-dollar loans was to share the results from successful programs.[34] For example, it highlighted that safe, affordable, and feasible small-dollar lending does occur in mainstream financial institutions; that small-dollar lending can be part of a foundation for creating profitable relationships; and that defaults on these loans are similar to defaults on other types of unsecured credit. Finally, participants in the federal banking regulator discussion group noted that the regulators have shared leading practices at their bi-annual National Interagency Community Reinvestment Conference hosted by the Board of Governors of the Federal Reserve System (FRB), FDIC, OCC, and the CDFI Fund. A participant in the nonfederal banking regulator discussion group noted these conferences provide many valuable resources.

Offering Financial Incentives to Encourage Basic Banking Services and Small-Dollar Loans

In the literature we reviewed and interviews, stakeholders suggested that federal and state governments could offer financial incentives to encourage banks to provide basic banking services and small-dollar, nonmortgage consumer loans. Suggested options include:

[33]In 2001, the North Carolina State Employees' Credit Union began offering a payday loan alternative program known as the Salary Advance Loan program after noticing increased use of payday loans by its members. The program offers a revolving loan, with a maximum outstanding balance of $500, offered at an APR of 12 percent. Thus, on a $500, 2-week loan, the charge is less than $2.50. The loans must be repaid in full on the borrower's next payday through automatic deduction. Since the program's inception, the credit union has made a total of $305,405,278 in loans, generating $1,919,097 in interest income, while experiencing $707,474 in net charge-offs and earning an estimated return of 7.76 percent.

[34]Federal Deposit Insurance Corporation, "A Template for Success: The FDIC's Small-Dollar Loan Pilot Program."

- **Providing financial subsidies.** Stakeholders recommended financial subsidies as a way to encourage provision of basic banking services and small-dollar loans. For example, one article noted that efforts by banks to expand access to credit in LMI communities are costly, resulting in a lower profit margin or even a net loss, and suggested that the government consider providing incentives to offset these low margins.[35] Representatives from an industry group additionally suggested that the government could promote tax credits.

  Several discussion group participants expressed support for government subsidies to offset low profit margins. For example, one participant in our advocacy discussion group explained that having access to low-cost capital or grant funds—such as the CDFI Fund—has been a major catalyst for innovation in the small-dollar lending arena. Another participant noted small-dollar loans are difficult to make profitably, and a subsidy or tax break for financial institutions that make them might encourage more such loans. A participant in our industry discussion group noted that her bank received CDFI Fund awards that helped support the launch of its small-dollar loan programs. Similarly, two participants explained that while subsidies are not a long-term solution, they can be a useful way to help an institution initiate small-dollar loan programs.

  However, other discussion group participants expressed reservations about both the sustainability and likelihood of this option. For example, two participants in the industry discussion group noted although this change would have the most impact, it was very unlikely to be implemented and would be difficult to sustain. Another participant felt that not only was it not sustainable but it was also not an appropriate policy because not every product and service an institution offers must be profit maximizing or profitable.

  In addition, several stakeholders suggested that local and state legislative incentives have generally been ineffective in encouraging financial institutions to offer more loans. For example, a participant in our advocacy discussion group explained that a legislative requirement for a safe account was ineffective largely due to lack of a data reporting requirement. In addition, a participant in our nonfederal

[35]M. Willis, "It's the Rating, Stupid: A Banker's Perspective on the CRA," in *Revisiting the CRA: Perspectives on the Future of the Community Reinvestment Act* (Boston and San Francisco: A Joint Publication of the Federal Reserve Banks of Boston and San Francisco, 2009), 59-70.

banking regulator discussion group explained that while there have been efforts in places like Philadelphia, San Diego, and Cleveland to encourage financial institutions to lend to LMI individuals in exchange for receiving deposits from the government, in at least one case (New York City) these incentives were found to be unconstitutional. Finally, in regards to offering financial incentives, one federal banking regulatory official told us it would seemingly be a conflict of interest for regulators to both oversee financial institutions' CRA activities as well as offer them financial incentives to improve their CRA performance.

- **Granting relief or imposing penalties based on CRA ratings.** One paper stated that given the consolidation in the financial services industry, the penalties for noncompliance with CRA should be revised.[36] Possibilities it noted were charging non-compliant institutions penalty rates on loans from the discount window or charging fines as a penalty for non-compliant institutions. Alternatively, another paper stated that banks that achieve an Outstanding CRA rating could be allowed some sort of financial (perhaps lower deposit insurance premiums) or regulatory relief (such as more time between CRA examinations).[37]

[36]L. Cohen and R. Agresti, "Expanding the CRA to All Financial Institutions," 134-137.

[37]M. Willis, "It's the Rating, Stupid: A Banker's Perspective on the CRA," 59-70.

Appendix V: Comments from the Department of the Treasury

DEPARTMENT OF THE TREASURY
WASHINGTON, D.C. 20220

January 12, 2018

Alicia Puente Cackley
Director
Financial Markets and Community Investment
U.S. Government Accountability Office
441 G Street NW
Washington, DC 20548

Dear Ms. Puente Cackley:

Thank you for the opportunity to review the draft report entitled *Community Reinvestment Act* (the Report). This letter provides the official response of the Department of the Treasury (Treasury).

The Report recommends that Treasury consider the options outlined in the Report as part of Treasury's review of the Community Reinvestment Act framework. Treasury accepts the recommendation and will consider the options outlined in the Report.

Thank you once again for the opportunity to review the Report. We look forward to continuing to work with your office in the future.

Sincerely,

Christopher Campbell
Assistant Secretary
Financial Institutions

Appendix VI: GAO Contact and Staff Acknowledgments

GAO Contact

Alicia Puente Cackley, (202) 512-8678 or cackleya@gao.gov

Staff Acknowledgments

In addition to the contact named above, Paige Smith (Assistant Director); Deena Richart (Analyst in Charge); Lawrence Crockett, David Dornisch, Jonathan Harmatz, Gina Hoover, Angela Kaylor, Courtney LaFountain, John McGrail, Jon D. Menaster, and Jim Vitarello made key contributions to this report. Also contributing were Robert Letzler, John Mingus, Dae Park, Tovah Rom, and Jena Y. Sinkfield.

GAO's Mission

The Government Accountability Office, the audit, evaluation, and investigative arm of Congress, exists to support Congress in meeting its constitutional responsibilities and to help improve the performance and accountability of the federal government for the American people. GAO examines the use of public funds; evaluates federal programs and policies; and provides analyses, recommendations, and other assistance to help Congress make informed oversight, policy, and funding decisions. GAO's commitment to good government is reflected in its core values of accountability, integrity, and reliability.

Obtaining Copies of GAO Reports and Testimony

The fastest and easiest way to obtain copies of GAO documents at no cost is through GAO's website (http://www.gao.gov). Each weekday afternoon, GAO posts on its website newly released reports, testimony, and correspondence. To have GAO e-mail you a list of newly posted products, go to http://www.gao.gov and select "E-mail Updates."

Order by Phone

The price of each GAO publication reflects GAO's actual cost of production and distribution and depends on the number of pages in the publication and whether the publication is printed in color or black and white. Pricing and ordering information is posted on GAO's website, http://www.gao.gov/ordering.htm.

Place orders by calling (202) 512-6000, toll free (866) 801-7077, or TDD (202) 512-2537.

Orders may be paid for using American Express, Discover Card, MasterCard, Visa, check, or money order. Call for additional information.

Connect with GAO

Connect with GAO on Facebook, Flickr, LinkedIn, Twitter, and YouTube. Subscribe to our RSS Feeds or E-mail Updates. Listen to our Podcasts. Visit GAO on the web at www.gao.gov and read The Watchblog.

To Report Fraud, Waste, and Abuse in Federal Programs

Contact:

Website: http://www.gao.gov/fraudnet/fraudnet.htm
E-mail: fraudnet@gao.gov
Automated answering system: (800) 424-5454 or (202) 512-7470

Congressional Relations

Orice Williams Brown, Managing Director, WilliamsO@gao.gov, (202) 512-4400, U.S. Government Accountability Office, 441 G Street NW, Room 7125, Washington, DC 20548

Public Affairs

Chuck Young, Managing Director, youngc1@gao.gov, (202) 512-4800
U.S. Government Accountability Office, 441 G Street NW, Room 7149
Washington, DC 20548

Strategic Planning and External Liaison

James-Christian Blockwood, Managing Director, spel@gao.gov, (202) 512-4707
U.S. Government Accountability Office, 441 G Street NW, Room 7814,
Washington, DC 20548

Please Print on Recycled Paper.