Redlining - The Fight Against Discrimination in Mortgage Lending

Freddi L. Greenberg

Follow this and additional works at: http://lawecommons.luc.edu/luclj
Part of the Banking and Finance Law Commons

Recommended Citation
Available at: http://lawecommons.luc.edu/luclj/vol6/iss1/4
Redlining—The Fight Against Discrimination in Mortgage Lending

INTRODUCTION

On Saturday, June 22, 1974, forty residents of Chicago's southwest side assembled at the offices of a local savings and loan association to demand that the institution disclose information regarding its lending activities in the Chicago area for the preceding four years. The disclosure demand was part of an effort to determine whether the association was "redlining" the area in which it was located by refusing to loan money for the purchase and improvement of homes in that area. This neighborhood is one of several Chicago neighborhoods where residential financing has been unavailable, causing residents to charge local financial institutions with redlining.

Pressure has also been exerted upon state and local governments to regulate mortgage lending practices. This pressure has not been without results. Allegations of redlining by Chicago area financial institutions have resulted in the amendment of an ordinance and

2. Although savings and loan associations are not the only source of residential financing, they are the primary source of such funds. At the end of 1973, savings and loan associations held 48.4 per cent of all loans on one to four family homes held by the private sector in the United States. This percentage excludes residential loans held by the United States government and federal agencies such as the Federal National Mortgage Association, the Federal Home Loan Mortgage Corporation, and the Farmers' Home Administration. The total value of mortgages held by the savings and loan associations was $186.8 billion as compared to $67.2 billion in mortgages held by commercial banks. UNITED STATES LEAGUE OF SAVINGS ASSOCIATIONS, '74 SAVINGS & LOAN FACT BOOK 37-38 (1974).

Because of the predominance of savings and loan associations in the home financing field, this note will focus primarily upon redlining as practiced by state and federally chartered savings and loan associations.

Savings and loan associations have historically specialized in conventional loans rather than mortgages insured by the Federal Housing Authority or the Veterans Administration. At the end of 1973, conventional loans totalled 87.2 per cent of all mortgages financed by savings and loans. Id. at 78-79.

Because of the more favorable terms offered to borrowers by conventional rather than insured financing, the current furor over redlining in the Chicago area centers around the failure of financial institutions to grant conventional loans. Therefore, this note will be limited to a treatment of discrimination in the granting of conventional mortgages. For a thorough treatment of problems involved in loans insured by the Federal Housing Administration, see B. BOYER, CITIES DESTROYED FOR CASH (1973). In addition, see McClaughry, The Troubled Dream: The Life and Times of Section 235 of the National Housing Act, 6 LOYOLA U. CHI. L.J. 1 (1975).
the passage of a resolution by the Chicago City Council, the promulgation of an anti-redlining regulation by the Illinois Commissioner of Savings and Loans, introduction of remedial legislation in the state legislature, and investigations of the problem by the Illinois Legislative Investigating Commission and the Governor's Commission on Mortgage Practices.

DEFINITION OF REDLINING

The term redlining is derived from the practice of marking maps with red lines surrounding areas which are believed to present bad risks to mortgage lenders. This practice is not a new one and is not confined to private financial institutions. Since the period before World War II, the Federal Housing Administration has redlined certain areas. Insurance companies also use this method of designating areas of a city in which insurance policies are available only at higher premiums. Redlined areas are usually older city neighborhoods or suburbs, and are often areas which are changing in racial composition.

Besides the refusal to grant mortgages in particular areas, redlining, consists of several more subtle practices. The terms of mortgages which are available may be less favorable than terms of mortgages in other areas. For example, mortgages in redlined areas are often available only at higher interest rates, for shorter terms, or with a requirement of a larger downpayment than those required for mortgages in purportedly more desirable areas. Some savings and loan associations which give mortgages on suburban property for downpayments of 5 per cent to 20 per cent require downpayments of 40 per cent in redlined areas. Other lending institutions, adopting

---

4. CHICAGO CITY COUNCIL JOURNAL 8268 (May 29, 1974).
11. Phone conversation with Jordan H. Bodenstein, Counsel, Illinois Legislative Investigating Commission, Oct. 11, 1974. Two Chicago areas which have allegedly been redlined are Rogers Park and Austin. ILLINOIS LEGISLATIVE INVESTIGATING COMMISSION, "REDLINING" ALLEGED DISCRIMINATION IN HOME IMPROVEMENT LOANS 3 (1974).
the seemingly neutral criterion of building age as the sole basis for refusing to give mortgages, effectively make mortgages unavailable in older neighborhoods.\textsuperscript{13}

Another aspect of redlining is the practice of giving forward commitments of mortgage money. Some savings and loan associations commit large sums of money for future mortgages on multi-million dollar subdivisions. A developer is guaranteed that his customers will have access to mortgage money at attractive interest rates. In Cook County, Illinois, approximately two-thirds of available mortgage funds are committed to developers before mortgages for homes in the developers' subdivisions are actually requested, effectively placing that portion of the available mortgage money out of the reach of the individual who is seeking a mortgage on his own.\textsuperscript{14}

The final aspect of redlining is the relocation of neighborhood banks and savings and loan associations out of the neighborhoods which they were chartered to serve, leaving no sources of mortgage money in the area. An institution may actually relocate or may establish a "branch" office in a more desirable neighborhood, later phasing out the original facility. One area on Chicago's west side, with a population of 300,000, was left without a local financial institution when the single neighborhood bank moved to downtown Chicago.\textsuperscript{15} Federal regulations concerning branching and relocation of savings and loan associations emphasize the impact of the move upon the new areas to be served, but do not consider whether the move will adversely affect the institutions' original service areas.\textsuperscript{16} State regulations on this point indicate a greater willingness to consider the impact of such a move on an association's original service area.\textsuperscript{17}

**Effects of Redlining**

Redlined areas are generally those which are changing in racial

\textsuperscript{13} One Chicago savings and loan association informed a prospective home owner that he would be unable to get a mortgage on a forty year old house and that the association did not like to loan money on homes over 15 years old. *Id.* at 30.

\textsuperscript{14} Illinois Legislative Investigating Commission, Hearings on Redlining, Prepared Testimony of Mary Lou Wolff, President of Citizens' Action Program, August 1, 1974 (copy on file in Loyola Law Journal office).

\textsuperscript{15} Illinois Legislative Investigating Commission Hearings on Redlining, Testimony of Father Albin Ciciora, July 25, 1974, at 44.


\textsuperscript{17} Ill. Savings and Loan Reg., art. X (1973).
composition or viewed as deteriorating. The unavailability of mortgage money discourages new residents from moving into these areas. Older residents who are unable to obtain loans to improve their property may move elsewhere, selling their homes for less than the actual value of the property.

The availability of mortgage money is crucial to the vitality of a community. Because two-thirds to four-fifths of the cost of purchase or improvement of property is normally financed by borrowing, the unavailability of such funds means that construction, purchase, and rehabilitation of existing homes cannot occur.

Lack of investment funds and its accompanying effect of discouraging new residents and businessmen from moving into a neighborhood places a burden upon local government. The shift of trade from neighborhood stores to suburban shopping centers reduces the city's sales tax revenue. The expense of providing services to city residents rises, and costly rehabilitation programs may be necessary. Therefore, a savings and loan association’s determination that an area is deteriorating may be a self-fulfilling prophecy.

THE FEDERAL HOME LOAN BANK STUDY

On February 21, 1974, the Federal Home Loan Bank of Chicago released a report summarizing savings and lending data received in a survey of savings and loan associations serving the Chicago area. The survey reported the total number and aggregate dollar amount of loans made between June 30, 1971 and June 30, 1973. Also reported were the number and aggregate amounts of savings deposits held by the institutions during this same period. The data were arranged by a zip code, but were not broken down by association.

Analysis of the Bank’s report indicates that in heavily redlined areas of metropolitan Chicago, an average of four cents a year was reinvested in the neighborhoods for every dollar deposited. In less heavily redlined older neighborhoods of the city, an average of eight cents was reinvested for every dollar deposited. Investment in suburban areas was 31 cents per dollar of deposits. Whereas total lending by

18. See note 11 supra.
20. Id.
reporting associations rose by 11.1 per cent between 1972 and 1973, and lending in the newer suburbs increased by 12 per cent, investment fell as much as 64 per cent in some Chicago neighborhoods which savings and loan associations have allegedly redlined.22

This study does not present a true picture of the lending practices of Chicago area savings and loan associations. Sixty-two local associations with assets totaling $5,448,500,706 were excluded from the survey because they failed to respond to the questionnaire or responded incompletely.23 In comparison, 127 participating associations had assets totaling $7,785,070,118.24 These figures indicate that some of the area's larger associations were not included in the survey results. Furthermore, the information was not broken down by institution, making it impossible to ascertain the extent to which individual institutions were practicing discrimination in lending.

SELF-HELP REMEDY FOR REDLINED COMMUNITIES

Because the directors of a mutually owned savings and loan association25 are elected by its members,26 it is theoretically possible for the members of an association which is redlining to nominate and elect directors who are committed to a change in the institution's lending policy.27 Customers of a mutually owned savings and loan association—borrowers and savers—are members of the association with voting rights.28 Such an association generally solicits a proxy from each member when a savings account is opened or when a loan is

24. Id.
25. Eighty-eight per cent of all savings and loan associations in the United States are mutually owned. ABA COMMITTEE ON SAVINGS AND LOAN ASSOCIATIONS, SECTION OF CORPORATION BANKING AND BUSINESS LAW, HANDBOOK OF SAVINGS AND LOAN LAW 12 (1973). All federally chartered savings and loan associations are mutually owned. 12 U.S.C. § 1464(b) (1973). Illinois law provides for capital stock and mutual associations. For a discussion of the differences between the two types of associations, see HANDBOOK, supra at 12-14.
27. Another method by which members of savings and loan associations have attempted to exert leverage over an association which is charged with redlining is to pledge that they will withdraw their savings if the associations do not change their lending policies. Citizens Action Program Action, July, 1974, at 4, col. 3.
28. Each member of a federally chartered savings and loan association is entitled to one vote per $100 of savings or fraction thereof on deposit. Each borrower is entitled to a single vote. No member may have over fifty votes. 12 C.F.R. § 544.1 (Supp. 1974).

Voting rights are the same under the Illinois Savings and Loan Act except that one vote is also granted to each holder of a permanent reserve share of a capital stock association. ILL. REV. STAT. ch. 32, § 741(d) (1973).
Directors of the association are elected by ballot of the members, usually at the association's annual meeting.20

A major obstacle for members attempting to exercise their voting rights in concert is the procedure which must be followed in solicitation of proxies. The Illinois Savings and Loan Act and the regulations of the Federal Home Loan Bank Board give each member the right to inspect an association's books only in so far as they pertain to his account.21 This right is substantially more limited than the right of corporate shareholders in most jurisdictions to inspect corporate books and to copy a list of names and addresses of other shareholders in order to communicate with them about corporation business.22

If a member of an Illinois chartered savings and loan association wishes to communicate with fellow members, he must submit a copy of the proposed communication to the State Commissioner of Savings and Loan Associations for a determination that it is "appropriate and truthful."23 The Commissioner may then direct the association to prepare and mail the communication to all of its members, at the expense of the requesting member.24 One problem presented by this provision is that no member may inspect an association's records to determine if loans are being made in the neighborhood. Therefore, a communication which a member has submitted in good faith, and which charges an institution with refusal to lend in its neighborhood may be determined by the Commissioner to be untruthful.

Although there is authority that members of federally chartered savings and loan associations have a right to inspect and copy membership lists for the purpose of soliciting votes for an election of directors,25 those associations may adopt a procedure which requires that

---

20. Federal regulations require that all savings and loan associations, state or federal, which are insured by the Federal Savings and Loan Insurance Corporation provide members with a revocable proxy, labelled in boldface type and printed on a separate sheet of paper, when an account is opened or a loan transacted. 12 C.F.R. § 569.2 (Supp. 1974). In 1973, 97.2 per cent of the assets of all state and federally chartered associations were insured by the Federal Savings and Loan Insurance Corporation. UNITED STATE LEAGUE OF SAVINGS ASSOCIATIONS, '74 SAVINGS & LOAN FACT BOOK 122 (1974).

21. Directors of federally chartered associations are elected by ballot for terms of 3 years, with approximately one-third of the board elected each year. 12 C.F.R. § 544.1(a)(5), (b)(5) (Supp. 1974).


23. ILL. REV. STAT. ch. 32, § 748(b) (1973).

24. Murphy v. Colonial Federal Savings and Loan Association, 388 F.2d 609 (2d...
communications among members be prepared and mailed by the association. According to this procedure, a member submits a proposed communication to the association's management for a determination that the subject matter is one which may be properly considered at a meeting of the association's members. If approved, the communication is then prepared and mailed, again at the expense of the member who submitted it.

In the only case to date construing the federal by-law, plaintiffs were members of a local community organization who attempted to circumvent the procedure prescribed by the by-law for communication with other members. They claimed that the by-law was inadequate for their purposes because they wished to communicate personally with other members. The court granted plaintiffs' motion for summary judgment on the grounds that the Federal Home Loan Bank Board's regulation which permits savings and loan associations to adopt the by-law does not preempt the federal common law. Judge Bauer remarked that the rights accorded an association's members by the by-law are substantially narrower than the rights accorded them by the common law. He therefore concluded that if the Federal Home Loan Bank Board had intended to limit members' rights of communication to those provided in the by-law, it would have so indicated. The court noted that plaintiffs had investigated the possibility of compliance with the by-law, and had found it too costly, but stated that even if the cost had been reasonable, plaintiffs' message could best be conveyed to their fellow members by face to face meetings. Similar decisions by other courts would appear to necessitate that the Federal Home Loan Bank Board clarify the purpose behind the optional by-law. For the moment, members of savings and loan associations which have adopted the by-law must follow the prescribed procedures unless they wish to challenge its provisions in court.

Besides following appropriate procedures for soliciting proxies from other members, those members of a savings and loan association

---

36. 12 C.F.R. § 544.6(g) (Supp. 1974).
37. Kupiec v. Republic Federal Savings and Loan Association, Civil No. 74 C 378 (N.D. Ill., Oct. 3, 1974). The court had previously denied plaintiffs' motion for a preliminary injunction on the grounds that permitting members to inspect the books of the association might interfere with the ordinary conduct of association business and that plaintiffs' attempt to arrange a face to face meeting of the members might offend other members of the association and cause the association irreparable harm. Kupiec v. Republic Federal Savings and Loan Association, 373 F. Supp. 1362 (N.D. Ill. 1974).
38. See note 35 supra.
who attempt to wage a proxy fight should also ascertain whether the association has adopted either of two additional optional by-laws. One by-law requires that advance notice of candidates nominated for directors be given to the association's secretary. The second by-law requires that the secretary be notified in advance of new business to be brought up at the association's annual meeting. Care must be taken to meet the required deadlines if such by-laws have been adopted.

The utility of proxy solicitation as a tool for eliminating redlining from a community is greatly dependent upon the size and nature of the savings and loan association involved. Because no member can have more than fifty votes, proxies must be solicited from a large percentage of the association's members. An association which has an exclusively neighborhood clientele is most likely to have a high percentage of members who are concerned with the association's lending policies in its immediate neighborhood. Even if the members fail to marshall enough votes to elect the directors they have nominated, a sufficient number of votes to demonstrate their strength to the institution's management may result in the slating of one of their candidates by the management in a future election.

EXISTING ANTI-REDLINING MEASURES

Chicago's Solution—The Depositary Ordinance

On June 25, 1974, the Chicago City Council passed a Municipal Depositaries Ordinance. The ordinance provided that a bank or savings and loan association could not become a depositary of Chicago's city or school funds without signing an anti-redlining pledge and disclosing extensive information about its residential lending practices.

---

39. 12 C.F.R. § 544.6(a) (Supp. 1974) provides for the nomination of directors by an appointed committee. Other nominations must be delivered to the secretary of the association at least 10 days prior to the annual meeting.
40. 12 C.F.R. § 544.6(b) (Supp. 1974) requires that new business to be discussed at the annual meeting be filed with the association's secretary at least 30 days prior to the annual meeting.
42. Although plaintiffs in Kupiec had only 11,000 votes within their control at the annual meeting, compared to the 300,000 votes in the hands of the association's proxy committee, the association management indicated that it was considering including some neighborhood residents in its next slate for board of directors. Marshall, Mortgage Redlining, Savings and Loan News, June, 1974, at 51.
43. CHICAGO, ILL., MUNICIPAL CODE ch. 7, §§ 7-30 to -40, as amended June 26, 1974.
44. This is the first time that savings and loan associations have been permitted to be depositaries of city funds. This is particularly important because it will provide additional money to be loaned as mortgages. Illinois Legislative Investigating Commission, Hearings on Redlining, Prepared Testimony of Alderman Dick Simpson, August 1, 1974 (copy on file in Loyola Law Journal office).
within the previous calendar year. The information was originally required to be broken down according to census tract.

When bids were opened to 199 eligible financial institutions on August 12, 1974, only three institutions bid for the city funds.\textsuperscript{45} Because several banks and savings and loan associations had indicated that they would be unable to compile the required information within the allotted time, the City Council retrenched and modified the ordinance at its August 21 meeting.\textsuperscript{46} The disclosure requirement and pledge were postponed to 1975. Whereas, the original ordinance required that lending data be disclosed by census tract, the revised ordinance permits 1975 lending data to be compiled by zip code or by census tract, requiring disclosure by census tract to begin in 1976. The effectiveness of this ordinance in discouraging redlining will not be measurable until the results of the 1975 and 1976 bidding are available.

A depositary bill was also considered by a committee of the Illinois State Legislature.\textsuperscript{47} The proposed state legislation was unsatisfactory in that it consisted of an anti-redlining pledge\textsuperscript{48} without requiring disclosure of lending data. Although compliance with such depositary laws is purely voluntary, the use of governmental funds may prove to be an attractive incentive to discontinue redlining during the current “credit crunch.” When the credit crunch has subsided, however, it is likely that the effectiveness of depositary laws will be reduced. Because of its voluntary nature, this type of statute does not present the pre-emption problems which arise when a state government attempts to regulate federally chartered savings and loan associations.\textsuperscript{49}


\textsuperscript{46} \textsc{Chicago, Ill., Municipal Code} ch. 7, §§ 7-34, 7-34.1, as amended, Aug. 21, 1974.

\textsuperscript{47} S. 1386, Ill. 78th General Assembly (1973-74). According to a telephone conversation with the bill's sponsor, Senator Harold Nudelman, on September 19, 1974, the bill remained in executive committee and must be re-introduced at the next session of the legislature.

\textsuperscript{48} The anti-redlining pledge was essentially the same as that required by the Chicago ordinance.

\textsuperscript{49} Courts have consistently held that regulation of federal savings and loan associations has been vested solely in the Federal Home Loan Bank Board and that such institutions are not subject to state laws relating to the regulation of savings and loan associations. \textit{See} People, Etc. v. Coast Federal Savings and Loan Association, 98 F. Supp. 311 (S.D. Cal. 1951); Springfield Institution v. Worcester Federal Savings and Loan Association, 329 Mass. 184, 107 N.E.2d 315 (1952).
The Illinois Regulation

On January 17, 1974, the Illinois Savings and Loan Commissioner promulgated a regulation prohibiting Illinois chartered savings and loan associations from varying the terms of mortgages because of the geographic location of the proposed collateral. Illinois thus became the first state in the United States to enact a statute or administrative regulation prohibiting the practice of redlining. On closer scrutiny, the regulation appears to be an exercise in futility.

The regulation requires that all Illinois savings and loans maintain records of loan applications which have been approved. Further, the Commissioner of Savings and Loans is empowered to require that a savings and loan association also retain records of rejected loan applications for a period of two years. The Commissioner may also require that the records of rejected loans be submitted to him. It was intended that the Commissioner would impose the additional record keeping requirement upon those associations which had been charged with redlining. To date only a handful of complaints have been received, and the Commissioner has determined that none of these allegations require further inquiry into the lending policies of the associations in question.

The Illinois anti-redlining regulation, which is dependent upon complaints by individuals whose loan applications have been rejected, presents the risk of random enforcement. It is unlikely that many citizens will take the trouble to report instances of redlining to the Commissioner of Savings and Loans because he lacks the power to provide them with mortgage money. A more effective system would be one in which all state chartered savings and loans were required to maintain records of rejected mortgage applications. These records could be periodically reviewed by the Commissioner's staff. This review could be conducted concurrently with the yearly examination which the Commissioner is required to make of the books of each Illinois chartered savings and loan association.

53. Id. art. VI, § 2(b).
54. Id. art. IV, § 3(b)(2).
55. Id. art. VI, § 2(b).
57. Id.
The Illinois regulations provide that a presumption of discrimination shall attach to a rejection of a mortgage loan which is unsupported by documentation which indicates that sound underwriting practices were used. Because savings and loan associations are not required to retain records of rejected loan applications until after a complaint is received, the Commissioner may be unable to determine the basis for the rejection of a complainant's application. It is unlikely that an association which has been charged with redlining and required to retain rejected loan applications would openly continue its discriminatory lending practices. Therefore, few, if any, charges of redlining will be substantiated under this regulatory scheme.

The anti-discriminatory regulations are silent with regard to sanctions applicable to savings and loan associations which engage in redlining. The Illinois Commissioner of Savings and Loans is empowered to institute a lawsuit to enforce state laws which are applicable to state chartered savings and loan associations. He may apparently follow the same procedure to enforce regulations which have been promulgated for the purpose of implementing the Illinois Savings and Loan Act. However, the poor response to the regulations by mortgage applicants and the difficulty of determining why a loan application was rejected render it unlikely that a charge of redlining will ever reach this stage.

The Federal Home Loan Bank Board Regulations

On April 21, 1972, the Federal Home Loan Bank Board adopted a regulation prohibiting discriminatory lending practices:

No member institution shall deny a loan or other service rendered by the member institution for the purpose of purchasing, constructing, improving, repairing or maintaining a dwelling . . . because of the race, color, religion, or national origin of

(a) An applicant for any such loan or any other service rendered by the member institution;
(b) Any person associated with such applicant in connection with such loan or other service or the purposes of such loan or other service;
(c) The present or prospective owners, lessees, tenants, or occupants of the dwelling or dwellings in relation to which such loan or other service is to be made or given; or
(d) The present or prospective owners, lessees, tenants, or

60. ILL. REV. STAT. ch. 32, § 841.2(e) (1973).
occupants of other dwellings in the vicinity of the dwelling or dwellings in relation to which such loan or other service is to be made or given.61

In an opinion letter dated March 21, 1974,62 the general counsel of the Federal Home Loan Bank Board indicated that, based on cases under Title VII of the Civil Rights Act of 196463 and cases under Title VIII of the Civil Rights Act of 1968,64 lending practices which are discriminatory in effect violate the anti-discrimination regulations regardless of the intent of the lender. Further analogizing from cases under the Civil Rights Acts, he indicated that statistical evidence which demonstrates a clear pattern of discrimination establishes a prima facie case of violation of the regulations, shifting to the defendant the burden of proof that discrimination is not being practiced. Noting that a genuine business purpose has been a defense to findings of discriminatory effect in cases under the Civil Rights Acts, he continued:

There is substantial legal precedent for the Board to presume that redlining that is discriminatory in effect is unlawful (without any countervailing business purpose) and to shift the burden to the institution to demonstrate some reasonable genuine business purpose for redlining. In any case, such a business necessity would not be established by the institution's unsubstantiated belief that no profitable loans could be made in a given area.65

While the federal regulations do not specifically prohibit redlining, they clearly indicate that redlining which has the effect of discriminating against any of the groups enumerated would constitute a violation of the regulations.

In order to protect those victims of redlining who are not members of the enumerated groups, the regulations would have to be expanded to include a prohibition against discrimination in residential financing which is based on the area in which the property is located. The regulations have been interpreted by the Federal Home Loan Bank Board to prohibit discrimination based on age, sex, and marital status of the potential borrower, on the rationale that such discrimination would impede the objective of promoting fair housing opportunity for all Americans.66 The same objective would be promoted by expand-

64. 42 U.S.C. § 3601 (1968).
ing the regulation to protect those individuals who are unable to finance their housing solely because of the areas in which they have chosen to live. Such a regulation would also be consonant with the purpose of providing for financing of homes by local institutions, a purpose which Congress expressed in authorizing the Federal Home Loan Bank Board to charter and regulate savings and loan associations. 67

The Federal Home Loan Bank Board has already instituted a record-keeping requirement which includes information on the location, by census tract or zip code, of the property which an applicant wishes to purchase or improve with the loan for which he has applied. 68 Though the Bank is seeking information as to the racial, ethnic, or religious affiliation of loan applicants, the data can also be used to ascertain whether an institution has established a pattern of refusing to loan mortgage money in a particular geographic area. Unlike the Illinois regulation, this record-keeping requirement applies to all financial institutions, and to all loan applications, whether or not they have been accepted. More significantly, the federal non-discrimination regulation and record-keeping requirement apply to all Federal Home Loan Bank members 69 whether they are chartered by the federal government or by a state government. 70 Therefore, the regulation applies to state and federally chartered institutions. Because savings and loan associations belonging to the Federal Home Loan Bank System hold 97.7 per cent of all the assets in the savings and loan business, 71 the regulation, if amended to prohibit redlining, will have a far-reaching effect. Because the record-keeping requirement is still being tested in several areas of the country, it is impossible to ascertain what

67. The relevant statutory provision states:

In order to provide local mutual thrift institutions in which people may invest their funds and in order to provide for the financing of homes, the Board is authorized, under such rules and regulations as it may prescribe, to provide for the organization, incorporation, examination, operation, and regulation of associations to be known as "Federal Savings and Loan Associations," and to issue charters therefore, giving primary consideration to the best practices of local mutual thrift and home-financing institutions in the United States.


69. 12 C.F.R. § 528.2 (Supp. 1974) provides that the federal non-discrimination regulation shall apply to all institutions which are members of a Federal Home Loan Bank. In 12 C.F.R. § 528.1 (Supp. 1974), the term "member institutions" is defined as all members except savings banks insured by the Federal Deposit Insurance Corporation, insurance companies, and the Federal Home Loan Mortgage Corporation.


71. UNITED STATES LEAGUE OF SAVINGS ASSOCIATIONS, 74 SAVINGS & LOAN FACT BOOK 112 (1974).
steps the Home Loan Bank Board will take when a violation of the regulation becomes apparent.\textsuperscript{72}

The success of the Federal Home Loan Bank Board in identifying discrimination by member institutions will not necessarily alleviate the major consequence of redlining—the unavailability or shortage of mortgage money in particular geographic areas. This aspect of the problem can only be solved by a program which, in addition to identifying institutions which discriminate, provides a source of money for those unable to obtain financing. The various means by which government can insure that such monies will be provided are discussed in the following section concerning potential state legislation. Similar legislation could be adopted on the federal level.

\section*{Proposals for Illinois Legislation}

Study of the redlining problem by two state commissions\textsuperscript{73} indicates that remedial legislation will be introduced in the Illinois General Assembly in the near future. Any attempt by the state to regulate federally chartered savings and loan associations will encounter difficulties because the field of regulation of the federal associations has been pre-empted by the Federal Home Loan Bank Board.\textsuperscript{74}

In order to determine the extent of redlining in Illinois and to evaluate the effectiveness of any remedial measures adopted, savings and loan associations must be required to keep records of all loan applications. The Federal Home Loan Bank Board has already instituted such a requirement in the Chicago area.\textsuperscript{75} Accordingly, such information is already available for members of the Chicago Home Loan Bank. Similar information can be obtained for non-members by expansion of the disclosure regulations promulgated by the Illinois Commissioner of Savings and Loans.\textsuperscript{76}

Further, public disclosure of each association's lending practices according to geographic area would

\textsuperscript{72.} A pilot program requiring that three different types of forms be filled out when loan applications are made, in three different groups of cities, was instituted on June 1, 1974 to continue for 6 months. This is part of an attempt to coordinate the Home Loan Bank Board's effort with similar record-keeping requirements to be implemented by the Federal Reserve System, the Federal Deposit Insurance Corporation, and the Comptroller of the Currency. These forms will be analyzed so that each agency can determine which form best serves its purposes and whether a coordinated effort should be continued. Chicago is part of this pilot project. Federal Home Loan Bank Board, Release 74-224 (March 22, 1974), 39 Fed. Reg. 18642 (1974).


\textsuperscript{74.} See note 49 supra.


\textsuperscript{76.} Ill. Savings and Loan Reg. art. VI, § 2 (1974).
enable members of the associations and citizens' groups to pressure redlining institutions to change their lending policies.

There are three general types of legislation which the state might adopt. The first type would result in an increase in the total amount of mortgage money which is available in the state, with an accompanying increase in the amount of money available for mortgages in redlined areas. A second type of legislation would directly involve the state in the provision of mortgage money or the insurance of mortgages for mortgagors unable to find financing due to redlining. The third type of legislation would involve state regulation of the mortgaging practices of savings and loan associations.

*Increased Availability of Mortgage Money*

Legislation which would result in an increase in the amount of available mortgage money includes:

1. Raising the state usury ceiling;
2. Rewarding those savings and loan associations which do not redline by allowing them tax credits or lowering their reserve requirements; and
3. Purchase by the State of Illinois of mortgages which were made in the past at lower interest rates, in order to free additional money to be loaned at current interest rates.

All of these would increase the total amount of mortgage money available in the state and consequently provide more money for lending in redlined areas. Data on the forward commitment of mortgage money by savings and loan associations indicates, however, that substantially more money is available than is being loaned in redlined areas. Therefore, there is no guarantee that any additional available mortgage money would be invested in these areas.

Furthermore, the lowered reserve requirement would offer no incentive to those Illinois savings and loan associations which are members of the Federal Savings and Loan Insurance Corporation if the state reserve requirement were lower than that corporation's reserve requirement. Because 97.2 per cent of all assets of savings and loan associations in the United States are insured by the Federal Savings and Loan Insurance Corporation, few Illinois associations would be af-

---

77. See text accompanying note 14 *supra.*
79. UNITED STATES LEAGUE OF SAVINGS ASSOCIATIONS, '74 SAVINGS & LOAN FACT BOOK 122 (1973).
fected by a lowered state reserve requirement.

Direct State Involvement in Granting Mortgages and Mortgage Insurance

The State of Illinois could become directly involved in combatting redlining either as a:

1. Direct lender or
2. An insurer of privately financed mortgages.

This would benefit prospective mortgagors who have been victims of redlining by enabling them to obtain financing.

Availability of state funds to those persons who have attempted to find residential financing and have been unsuccessful would offer an incentive to citizens to report instances of redlining to the state, thereby facilitating the enforcement of the Illinois anti-redlining regulation. Alternatively, direct state loans could be made generally available in redlined areas.

A variation of direct loans funded by the state has been instituted by the Illinois Housing Development Authority. Under that program, $22.9 million in mortgage money has been made available to 20 of Chicago’s financial institutions. The institutions must match the money with their own funds. Funded by tax-exempt securities, this “loan to lenders” program is an attempt to place new mortgage money in redlined areas of Chicago.

A state program of mortgage insurance would face the same problems encountered by the Federal Housing Administration in its mortgage insurance programs. Insured mortgages provide incentives for mortgagors to foreclose. This is particularly true if the insurer pays the cost of foreclosure. While conventional lenders frequently go to great lengths to avoid foreclosure, allowing mortgagors to be as many as ten months delinquent in their payments, Federal Housing Authority insured mortgages are often foreclosed if payments are 30 days overdue. Upon foreclosure, the insurer reimburses the mort-

---

82. Chicago Real Estate Advertiser, June 21, 1974, at 1, col. 3.
83. For a thorough treatment of the problems involved in the administration of insured mortgages through the Federal Housing Administration, see B. Boyer, Cities Destroyed for Cash (1973) and McLaughrly, The Troubled Dream: The Life and Times of Section 235 of the National Housing Act, 6 Loyola U. Chi. L.J. 1 (1975).
84. Illinois Legislative Investigating Commission Hearings on Redlining, Testimony of John Waner, August 1, 1974, at 93.
85. Id. at 88-92.
gagee for the amount invested in the mortgage.

A better alternative would be an insurance program which insures the mortgagor against the inability to meet his mortgage payments. This would offer no incentive to the mortgagee to foreclose. Both types of insurance, however, suffer from the defect of encouraging savings and loans to be less prudent in evaluating the prospective mortgagor's financial standing than if the application had been for a conventional loan.

**State Regulation of Savings and Loan Associations**

State regulation of mortgaging practices of savings and loan associations would include:

1. Periodic renewal of the charters of Illinois savings and loan associations contingent upon proof that they do not practice redlining;
2. Refusal to allow Illinois savings and loan associations to relocate or branch if such actions would deprive their original neighborhoods of needed mortgage money;
3. A requirement that associations institute affirmative lending programs; and
4. The creation of an assigned risk mortgage pool.

This type of regulation would be inapplicable to federally chartered associations, although similar provisions could be adopted by the Federal Home Loan Bank Board.

Periodic renewal of charters, conditioned on proof of non-discriminatory lending practices, would require identification of redlined areas and development of standards regarding the amount of mortgage money an institution should be lending in a particular area. Similarly, statistical data would be necessary to administer a program which conditions branching and relocation of associations on the availability of mortgage money in the association's original service area. The effect of either type of legislation would be limited to state chartered institutions. Finally, both of these proposals would require that small neighborhood savings and loan associations bear whatever financial risks are attendant upon lending in redlined areas, possibly endangering the security of their members' savings deposits.

In addition, the state could require savings and loan associations to adopt affirmative lending programs. Such programs would, of course,
be limited by the general availability of mortgage money. Under this plan, associations would be required to seek out mortgagors in their communities and even advertise the availability of funds for neighborhood mortgages. While this type of program would contribute to the revitalization of redlined areas by encouraging people to purchase homes there, it suffers from the disadvantage of placing a burden on neighborhood savings and loan associations. As in the case of the two preceding legislative proposals, adoption of this alternative would require the identification of redlined areas and the formulation of standards to evaluate the adequacy of each association's lending performance in those areas. Such procedures would further delay the availability of mortgage money to victims of redlining.

Finally, the best alternative in this category of legislation is the creation of an assigned risk mortgage pool to be administered by the state.\textsuperscript{87} This type of plan would allocate the risk of lending in redlined areas among all the savings and loan associations in a particular county. Mortgages would be granted to those individuals who had been refused funding by three or more institutions because of the location of the property they wished to purchase. Associations would be required to participate in varying degrees, depending upon the total amount of their assets. The financial burden would thus be removed from small, neighborhood associations located in redlined areas.

To insure that participating associations do not falsify the credit rating of the mortgagor or the condition of the collateral in order to avoid lending in redlined areas, state supervision of the appraisal of collateral and the evaluation of mortgagors is essential. Because persons desiring mortgages from the pool would have to report redlining to the state agency administering the program, creation of an assigned risk mortgage pool would have the incidental effect of aiding enforcement of the state's anti-redlining regulation.

The most effective type of state remedy for redlining is either an assigned risk mortgage pool or a program in which the state acts as a mortgagee. In either case, individuals who have been victims of redlining would be provided with an immediate source of mortgage money. The availability of mortgage funds would tend to encourage

\textsuperscript{87} Illinois has adopted a similar assigned risk plan to provide automobile insurance for those persons who are considered to present such high risks that they are unable to obtain automobile insurance. ILL. REV. STAT. ch. 95½, § 7-501 (1973). The Chicago City Council adopted a resolution recommending that the State of Illinois create an assigned risk mortgage pool. CHICAGO CITY COUNCIL JOURNAL 8268 (May 29, 1974).
the purchase and rehabilitation of homes in city neighborhoods, helping to reverse the effects of redlining. Both types of legislation would effectively combat redlining by state chartered associations if coupled with a strengthened state anti-redlining regulation which includes a requirement that all state savings and loan associations maintain records of all loan applications. However, the state’s inability to regulate federally chartered savings and loan associations underscores the need for state legislation which provides mortgage money for home purchasers, and offers relief to victims of redlining, whether they have been refused financing by state or federally chartered associations.

CONCLUSION

Just as Americans are concerned about recycling cans and bottles, the time is ripe for a program which recycles urban neighborhoods. The continued unavailability of mortgage money for the purchase and rehabilitation of homes in those neighborhoods contributes to the flight to the suburbs. If this trend is not reversed, many populated urban areas may ultimately be reduced to blocks of abandoned buildings which will become habitable only at great expense. To avoid this eventuality, mortgage money must be made available in redlined areas. To date, attempts to control redlining have proven inadequate. In order to reverse the flow of mortgage money out of redlined neighborhoods, governmental priorities must be re-evaluated and a commitment made to encourage and assist individuals wishing to purchase or improve homes in those urban areas.

FREDDI L. GREENBERG