NATIONAL COMMUNITY REINVESTMENT COALITION NCRC

January 5, 2006

Office of the Comptroller of the Currency
250 E Street SW, Mail Stop 1-5
Washington DC 20219
RE: Docket No. 05-17

Jennifer J. Johnson
Secretary
Board of Governors of the Federal Reserve System
20th Street and Constitution Avenue NW
Washington DC 20551
Docket No. OP-1240

Robert E. Feldman
Executive Secretary
Attention: Comments, RIN 3064-AC97
Federal Deposit Insurance Corporation
550 17th Street, NW
Washington DC 20429

To Whom it May Concern:

The National Community Reinvestment Coalition (NCRC), the nation's economic justice trade association of 600 community organizations, supports the proposed Questions and Answers that direct bank financing and low-cost services to low- and moderate-income communities. NCRC appreciates that the federal banking agencies have clarified how banks will receive favorable consideration in their Community Reinvestment Act (CRA) exams for financing community development activities in geographical areas impacted by natural disasters. While we are pleased that the federal agencies direct banks to focus on low- and moderate-income families in areas impacted by disasters, we are concerned that other proposed questions divert bank financing to middle- and upper-income housing. The agencies must implement CRA in a manner that maintains the law's central objective of ending redlining and expanding access to credit for low- and moderate-income families and communities.

Designated Disaster Areas

NCRC supports the agencies' proposal that banks will receive points on their CRA exams for financing community development in geographical areas impacted by disasters for up to one year after the expiration of official federal or state designation of disaster status (Proposed Q&A .12g4ii-1). Community development financing takes considerable time to plan and implement, meaning that the one year of additional time is important for geographical areas like the Gulf Coast region that have been devastated by natural disasters. However, the planning and implementation for the community development activity must have genuinely started within the time period of disaster designation, not one day or some other short time period before the expiration of the time period. The examiners should not tolerate "gaming" or manipulation of the time periods on exams.

The one year lag time is long enough for both designated disaster areas and underserved or distressed census tracts. Longer time periods could allow manipulation of CRA exams in which banks seek CRA points for large amounts of financing in former disaster areas that have less pressing needs for the financing as time has elapsed from the disaster. Also, the expiration of the official disaster time period is a clear standard. "Periods of assistance" or some other time frame for designating disaster area status verges into creating time periods of uncertain length that become difficult for the planning efforts of both banks and community organizations.

NCRC applauds the agencies for providing more "weight" or credit to community development activities that are most responsive to the needs of low- and moderate-income individuals that have been impacted by the natural disaster. We ask you, however, to strengthen the emphasis on projects benefiting low- and moderate-income families and communities. The proposed Q&A states that more weight will be awarded to community development activities that are most responsive to credit needs, including those of low- and moderate-income individuals or neighborhoods (Proposed Q&A .12g4ii-2). We ask you to change "including" to "particularly." One word can make a large difference in ensuring that more weight or CRA points are provided to community development activities benefiting low- and moderate-income families and communities.

Your proposal to provide CRA points for investments that benefit low- and moderate-income families displaced by disasters promises to be very beneficial to areas receiving a large influx of families resettling in the wake of Hurricane Katrina and future natural calamities. The proposed Q&A, however, is awkward in that it awards CRA points for investments in entities serving resettling families. Couldn't the Q&A be phrased to say that community development loans, qualified investments, and community development services benefiting resettling low- and moderate-income families and geographical areas receiving significant influx of families will receive CRA points?

Low-Cost Services

The proposed questions on community development services provide an important emphasis on low-cost banking services for low- and moderate-income consumers. Your proposed Q&A's specifically extol the development of "low cost bank accounts," "free government check cashing," "reasonably priced remittances services in connection with a low cost account," and "electronic benefit transfers" as means to decrease costs for lower income consumers and increase their access to financial services (Proposed Q&A .12i).

Low-cost checking accounts, electronic transfers, remittances, and other services provide critical alternatives to payday loans and other high cost fringe products. Low cost banking services enable low-income consumers to save and build wealth in contrast to usurious products that strip wealth. Once these proposed questions are finalized, we hope that the agencies provide CRA points for low cost banking services and also penalize banks on CRA exams for abusive products such as bounce protection, whose wealth stripping features are not advertised clearly to consumers. In order to receive points for low cost banking services and products, it is not sufficient for the banks to merely offer these products. Banks must be able to demonstrate that significant numbers of low- and moderate-income borrowers actually use their low-cost products.

Intermediate Small Banks or Mid-Size Banks

We ask that you clarify the CRA exam criterion for mid-size banks with assets between $250 million to $1 billion that assesses their provision of services through branches and other facilities. You must clarify that this exam criterion includes an examination of the number and percent of branches in low- and moderate-income communities.

The proposed question now states that providing services through branches count as community development services (Proposed Q&A .12i and Q&A .26c3-1). This is a vague criterion that does not necessarily mean that the examiners will be scrutinizing the number and percent of branches in lower income communities. The Q&A can be rephrased to say the "*provision of branches* and the provision and availability of services to low- and moderate-income individuals including through branches and other facilities located in low- and moderate-income areas." Just adding the phrase "provision of branches" can ensure that CRA examiners scrutinize the number and percent of mid-size branches in low- and moderate-income communities. Placing branches in low- and moderate-income communities is vital since a recent Federal Reserve study shows that racial disparities in high cost lending is less when banks conduct the lending through branches as opposed to using brokers.[1]

We applaud your proposed question and answer that reiterates that mid-size banks must offer community development loans, investments and services. Mid-size banks cannot ignore one or more of these activities (Proposed Q&A 26c 4-1). When determining the adequate level of community development activities, community needs rather than "opportunities" for engaging in community development must be the primary consideration. "Opportunities" is a slippery criterion that could be used to excuse low levels of community development activities in communities without an established infrastructure for community development. In communities without a community development infrastructure, banks should be expected to work with the public and non-profit sectors to develop an infrastructure. In addition, a CRA examiner cannot rely only on bank assessments of local community development needs as hinted at in proposed Q&A .26c4-1. The CRA examiner must collect assessments of community development needs conducted by community organizations and local government agencies.

[1] Robert B. Avery, Glenn B. Canner, and Robert E. Cook, *New Information Reported under HMDA and Its Application in Fair Lending Enforcement*, Federal Reserve Bulletin, Summer 2005, http://www.federalreserve.gov/pubs/bulletin/2005/05summerbulletin.htm

Upper-Income Housing

We oppose the proposed question and answer that provides CRA points for financing middle- and upper-income housing developments in distressed rural middle-income census tracts or designated disaster areas (Proposed Q&A .12g4-2). Elsewhere in the existing Question and Answer document and in your proposed questions, the agencies provide credit for mixed-income housing developments. Mixed-income housing helps to overcome segregation by income and is an activity worthy of CRA points if the housing contains a significant number of low- and moderate-income families.

You explain that middle- and upper-income housing in distressed or designated disaster areas can provide benefits to low- and moderate-income people by attracting a major employer that also employs low- and moderate-income people. This is an indirect and uncertain benefit. Even if the employer initially employed significant numbers of lower income workers, it is not clear that the employer would continue to do so if changes in the overall economy or the specific industry required automation or outsourcing. Moreover, your proposed Q&A directly contradicts existing Q&A .12(i) and 563e.12h-4 that states, "a loan for upper-income housing in a distressed area is not considered to have a community development purpose simply because of the indirect benefit to low- and moderate-income persons from construction jobs or the increase in the local tax base that supports enhanced services to low- and moderate-income area residents." In this existing Q&A, even the longer term benefits of an increase in the local tax base was discounted because the housing activity did not directly benefit low- and moderate-income people.[2]

The existing Q&As also emphasize the importance of mixed-income housing and discourage lenders from seeking CRA credit for loans financing middle- and upper-income housing. The federal agencies state in existing Q&A .22b2 & (3)-5 that loans for middle- and upper-income housing (single or multifamily) could receive CRA points if this housing is part of mixed-income housing that benefits communities by establishing "stabilized, economically diverse" neighborhoods. On the other hand, if no mixed-income housing plans exist and the loans for middle- and upper-income housing displace or otherwise significantly disadvantage low- and moderate-income people, then these loans would not receive CRA points. In addition, the very next question and answer (Q&A .22b4) states that mixed-income housing that reserves 65 percent of the units for low- and moderate-income households would receive more weight on CRA exams than mixed-income housing that sets aside 40 percent of the units for low- and moderate-income households.[3] It is clear that the existing Q&A encourages mixed-income housing and awards more CRA points for mixed-income housing that contains significant numbers of low- and moderate-income people. The existing Questions and Answers are

[2] Community Reinvestment Act; Interagency Questions and Answers Regarding Community Reinvestments, Federal Financial Institutions Examination Council, Federal Register, Vol. 66, No. 134, Thursday, July 12, 2001, p. 36626.
[3] Ibid., p. 36633.

appropriate since CRA was designed to benefit low- and moderate-income people and mixed-income housing provides direct benefits to low- and moderate-income people.

Another part of the proposed housing Q&A .12g4-2 does not provide credit for middle- and upper-income housing in underserved, rural middle-income census tracts unless the housing is mixed-income that also serves low- and moderate-income families. Your proposed Q&A's are simply contradictory; mixed-income housing is encouraged in underserved, thinly populated rural areas, but exclusively middle- and upper-income housing is permissible for CRA points in distressed, high poverty areas. Mixed-income housing that promotes economic diversity is urgently needed in high poverty areas as well as thinly populated locales. NCRC sees no reason for this contradiction and encourages you to eliminate the possibilities of banks receiving significant CRA points for financing middle- and upper-income housing. Furthermore, the proposed Q&A is so loosely worded that it would not prevent a bank from receiving CRA points for upper-income housing, even neglecting the needs of middle-income families. In order to be consistent with the purposes of CRA and existing precedent, we strongly urge you to provide points for mixed-income housing and also specify that the mixed-income housing should contain a significant number, and not a small number, of low- and moderate-income households.

Infrastructure Financing in Underserved Areas

In underserved areas, the agencies propose to award CRA points for financing infrastructure such as hospitals, industrial parks, or even the rehabilitation of schools, provided the infrastructure also services low- and moderate-income families (Proposed Q&A .12(g)(4)(iii)-3). The agencies are emphasizing financing infrastructure for rural underserved middle-income areas since these areas are sparsely populated, making it hard for the public and private sectors to finance infrastructure. While this proposed Q&A is reasonable, we ask you to specify that CRA examiners should quantify, as much as possible, how many low- and moderate-income families are expected to use the particular infrastructure in question. More CRA points should be awarded for infrastructure that has the most direct benefits to low- and moderate-income families. This procedure would be in line with the existing Q&A on mixed-income housing that directs examiners to weigh more heavily mixed-income housing with greater percentages of low- and moderate-income households.

Qualitative Factors on CRA Exams and Prior Period Investments

A proposed Q&A (.26c4-1) explains how qualitative factors will be considered on a mid-size bank's community development (CD) test. It states that in "some cases, a smaller loan may have more qualitative benefit to a community than a larger loan," if the loan is particularly responsive to community development needs. Another Q&A (.12t-1) states that a prior period investment could receive more points on a CRA exam than a current period investment if it is more "responsive to area community development needs."

It is true that smaller CD loans and investments can be more responsive to community needs than larger ones. For example, a CD loan for construction of a low-income housing development is more responsive than a larger CD investment in mortgage backed-securities (MBS), particularly if the MBS has been already traded on the secondary market. But qualitative factors should not excuse low levels of CD lending, investment, and services. Examiners can avoid erring too much on the side of qualitative factors by comparing the quantity of CD lending, investing, and services of banks of similar asset sizes operating in the same community.

Just like smaller CD loans, there could be prior period investments being more responsive than current period investments. However, providing credit for prior period investments should not be used to compensate for low levels of current period investments. A bank with a low level of current period investments should not be able to score higher than low satisfactory on the investment test. A high number of responsive prior period investments can make the difference between a high satisfactory or outstanding investment test rating on a CRA exam but it should not elevate the investment rating of a bank with a low level of investments in the current time period. Similarly, small levels of CD loans and investments should not result in higher than Satisfactory ratings on the CD test. Volume must count as well and should be used to separate the banks with Satisfactory from Outstanding ratings on the CD test.

Issues that Are Not Included in the Proposed Questions and Answers

Implementing New Regulatory Prohibition Against Discriminatory Practices

The federal agencies appropriately adopted a new provision to the CRA regulations stating that a bank's CRA rating will be adversely affected by evidence of discriminatory or other illegal practices. While we applaud strengthening the fair lending aspects of the CRA regulation, NCRC requests that the federal agencies add a new Q&A outlining how this provision will be implemented. Primarily, this Q&A would be implemented through fair lending reviews that probe for evidence of discriminatory or other illegal practices. We ask the regulators to indicate in a new Q&A that fair lending reviews would be automatic when there are high concentrations of subprime lending to protected classes.

A number of years ago, the Office of the Comptroller of the Currency (OCC) adopted a risk based approach to fair lending reviews. The OCC does not automatically conduct fair lending reviews for all banks during regularly scheduled CRA exams, but conducts a fair lending review only when certain risk factors are present. One such risk factor should be a high concentration of subprime loans to a protected class of borrowers. A high concentration of subprime loans may indicate steering and other discriminatory practices directed towards minorities, the elderly, women or traditionally underserved neighborhoods. The new Comptroller, John Dugan, in a recent speech hints that high concentrations of subprime lending is not desirable nor is "using the national bank charter as the primary vehicle for higher-cost loans."[4] Also, making high concentrations of subprime loans to regions recovering from natural disasters should also be a risk factor targeting a fair lending review. In this case, a lender may be taking advantage of a natural-disaster induced shortage of loans to flood an area with usurious loans.

List of Community Development Services and Qualified Investments: Add Post-Purchase Counseling and Microlending as Well as Tweaking Other Items

The federal agencies have added items to the examples of community development services and qualified investments. NCRC applauds the addition of investments in Rural Business Investment Companies (RBICs) as an example of qualified investments. NCRC members and other practitioners inform us that RBICs are a new and important vehicle for channeling investments into rural areas. Listing state and municipal bonds as an illustration of qualified investments is desirable. This item, however, should be modified to indicate that the bonds should primarily benefit low- and moderate-income families and/or low- and moderate-income communities. In addition, NCRC requests that the regulators add an explicit reference under community development services and investments to post-purchase counseling programs to ensure that borrowers can remain in their homes and do not fall prey to predatory lending. In addition, the regulators should add financial support of micro-lending programs in their new list of qualified investments.

Conclusion

The most effective way to expand access to credit to underserved borrowers is implementing rigorous and comprehensive CRA exams that maintain the focus on meeting the credit and deposit needs of low- and moderate-income borrowers and communities. A number of your proposed Q&As reinforce the focus on low- and moderate-income families and communities. These include the Q&As on designated disaster areas, low-cost banking services, and qualified investments. Parts of these questions should be strengthened to bolster the attention given to low- and moderate-income families and neighborhoods. In addition, we ask that you change the question on housing to eliminate the possibilities of banks earning CRA points by financing upper-income housing in rural areas, an outcome that would be contrary to the purpose of CRA. If you are responsive to our comments on the proposed Question and Answers, CRA exams will become more rigorous.

[4] Remarks of John C. Dugan, Comptroller of the Currency, December 1, 2005, http://www.occ.gov/ftp/release/2005-117a.pdf

Thank you for consideration of our comments. If you have any questions, please contact Josh Silver, Vice President of Research and Policy, or me on (202) 628-8866.

Sincerely,

John Taylor
President and CEO