September 2, 2010

MEMORANDUM TO: The Board of Directors

FROM: Sandra L. Thompson
Director
Division of Supervision and
Consumer Protection

Richard J. Osterman, Jr.
Acting General Counsel

SUBJECT: Joint Final Rule: Amendment to the Community Reinvestment Act Regulation

RECOMMENDATION

We recommend the Board approve and authorize for publication in the *Federal Register* the attached final rule revising the regulations implementing the Community Reinvestment Act (CRA). The FDIC would issue the rule with the Board of Governors of the Federal Reserve System, the Office of the Comptroller of the Currency, and the Office of Thrift Supervision (collectively, the Agencies).

The final rule would make two unrelated changes to the CRA regulations. The first would revise the regulation to reflect the Higher Education Opportunity Act (HEOA), which requires the Agencies to consider, as a factor in CRA evaluations, low-cost education loans provided by an institution to low-income borrowers. The second change would add a new regulatory provision to address a statutory provision that permits positive consideration of activities undertaken by a non-minority or non-women-owned financial institution in cooperation with minority- and women-owned financial institutions and low-income credit unions.

DISCUSSION

Background

The CRA requires the Agencies to assess the record of each insured depository institution in meeting the credit needs of its entire community, including low- and moderate-income neighborhoods, consistent with the safe and sound operation of the institution.

On June 30, 2009, a Joint Notice of Proposed Rulemaking (NPR) regarding CRA consideration for low-cost education loans and certain activities undertaken in cooperation with minority- and women-owned financial institutions was published in the *Federal Register* for a 30-day comment period. The Agencies together received 24 comments from a variety of commenters, including financial institutions, consumer groups, trade associations and an association of state lenders.

Final Rule Regarding Low-Cost Education Loans to Low-income Borrowers

The attached final rule is issued pursuant to Section 1031 of the HEOA, enacted August 14, 2008, which revised the CRA to require the Agencies to consider, in evaluating an institution, low-cost education loans provided by the institution to low-income borrowers.

Proposal

The proposed rule defined "low-cost education loans" to mean (1) education loans originated by an institution through a U.S. Department of Education loan program; or (2) any private education loan, including loans under a state or local education program, originated by an institution for a student at an "institution of higher education," with interest rates and fees no greater than those of comparable education loans offered through loan programs of the U.S. Department of Education. The proposal defined "low-income" consistent with the current definition in the CRA regulation to mean an individual income less than 50 percent of the area median income.

Definition of education loan

The proposed definition of "private education loan" included only loans made for post-secondary (beyond high school) educational expenses, not for primary or elementary education. Most commenters who addressed the issue supported the Agencies' proposal, although one trade association and one financial institution recommended a broader scope. After a review of the comments, staff recommends that the final rule cover only loans made for post-secondary educational expenses.

The Agencies requested comment on whether private education loans not made, insured, or guaranteed under a Federal, state, or local education program should be considered for CRA purposes. The majority of commenters who addressed this issue noted that many students and families are unable to cover the full cost of a college education relying only on government programs and need other types of funding, such as private, non-governmental loans to complete their education.

In the period between the end of the comment period and staff drafting this final rule, statutory changes were made to the Federal student lending program.[1] As a result of the legislation, after June 30, 2010, no new loans may be made under the Federal Family Education Loan Program (FFEL) which included education loans originated by financial institutions. No changes were made to the Federal Direct Loan program administered by the U.S. Department of Education. For these reasons, staff recommends the final rule not be limited to loans made or insured by a Federal or state program. In fact, the focus of any CRA evaluation going forward is likely to be primarily on private student lending.

The Agencies requested comment on whether to limit education loans to those originated by the institution, rather than purchased by the lender. Commenters were split on this issue; community groups supported a limit to those loans originated by institutions while

[1] Health Care and Education Reconciliation Act of 2010, Pub. L. No. 111-152, (2010)

financial institutions supported coverage of both originations and purchases. Staff believes that providing consideration only for loans originated by financial institutions provides an incentive to financial institutions to develop private education loan programs and thus recommends that the final rule limit consideration to low-cost private education loans originated by the financial institution.

Definition of low-cost

In the preamble to the proposed rule, the Agencies noted that the rates and fees allowed under the FFEL programs would typically be used to evaluate whether an institution's education loan would be low cost. Because of the statutory changes made to the FFEL program, and after a review of the comments, staff recommends that while the regulatory definition of low-cost loan be retained, the preamble language of the final rule reflect that the rates and fees allowed under the Federal Direct Loan program would be used to evaluate whether an institution's education loans would be low cost. To determine whether education loans have rates and terms that are no greater than the rates and terms on loans made under the Federal Direct Loan program, education loans made by financial institutions would be compared with comparable Federal direct loans. Because there are currently no variable rate loans made under the Federal program, the published rates used in servicing the existing portfolio would be the benchmark for private low-cost variable rate loans to low-income borrowers under this provision.

Definition of low-income

Under the proposed regulation, the term "low-income" was proposed to have the same meaning as that term is defined in the existing CRA rule: an individual income less than 50 percent of area median family income. Several commenters, including some community groups and several financial institutions or trade associations supported using the 50 percent benchmark as proposed. Several financial institutions and trade associations supported expanding the definition to cover both low-income and moderate-income borrowers.

After a review of the comments, staff recommends the Board retain the CRA standard, which focuses on low-income as 50 percent of the area median family income without further changes.

Comment Regarding Assessment Area

The proposed rule provided that the Agencies will consider low-cost education loans originated by a financial institution to low-income borrowers in its assessment area(s). The final rule would provide that the Agencies will consider such loans "particularly in its assessment area(s)." Similar to the analysis for loans to low- and moderate-income individuals generally, by adding, "particularly, " the Agencies would consider first whether a financial institution has adequately addressed the low-cost education loan needs of low-income borrowers in its assessment area(s) and, if so, would also consider such loans outside of its assessment area(s). Staff believes that the final rule may provide greater flexibility and additional incentives for financial institutions to provide low-cost education loan programs for low-income borrowers.

Final Rule and Comments Regarding Activities Undertaken in Cooperation with Minority- and Women-Owned Financial Institutions and Low-Income Credit Unions

The CRA permits the Agencies to consider as a factor, when they assess the community reinvestment record of a non-minority- or non-women-owned financial institution, such institution's capital investments, loan participations and other ventures undertaken by the institution in cooperation with minority- and women-owned financial institutions and low-income credit unions. Staff proposed to use this rulemaking to add clarifying language to the rule regarding these activities.

As with the current Interagency *Questions and Answers Regarding CRA* (Q&As), the proposed rule clarified that such activities need not benefit the assessment area(s) of the non-minority- and non-women-owned institution. Several consumer and community groups urged the Agencies to narrow the geographic scope by only providing favorable CRA consideration to investments in cooperation with minority- and women-owned financial institutions and low-income credit unions, if the majority-owned institution met the needs of its assessment area. The Agencies explained in the preamble to the Q&As, that the Agencies do not currently interpret the CRA to impose such a limitation. However, as indicated in the Q&As, the impact of such activities on majority-owned institution's CRA rating is determined in conjunction with its overall performance in its assessment area(s). Staff recommends the Board adopt the provision as proposed.

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Attachments