WOODSTOCK INSTITUTE

Advancing Economic Security and Community Prosperity

<u>VIA Email</u>

May 17, 2013

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Robert E. Feldman
Executive Secretary
Attention: Comments, Federal Deposit Insurance Corporation
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Re: Proposed Changes to Interagency Q&A
OCC: Docket ID OCC02013-0003
Federal Reserve: Docket No. OP-1456
FDIC: Attention: Comments on CRA Interagency Q&A

To Whom It May Concern,

I am contacting you on behalf of Woodstock Institute to provide comment on the proposed Interagency Questions and Answers (Q&A) Regarding Community Investment issued March 18, 2013. The revisions to the Q&A make some minor improvements to the implementation of the Community Reinvestment Act (CRA), such as additional ways to determine low- and moderate-income status of community development recipients, recognition of nonprofit board service, and clarifications on qualified investments and community development lending. We are concerned, however, that the proposals miss an opportunity to make necessary reforms to modernize CRA. Specifically:

- The proposed Q&A's attempts to clarify the permissibility of community development activities outside of current assessment areas would more effectively promote community engagement if assessment areas were redefined as where an institution has market share.

- While it is important to uphold the importance of community development lending, it should not be done at the expense of retail lending, the largest portion of the lending test. A more effective way of reaffirming community development work is to create a community development test.

- Regulators should make the services test more rigorous and meaningful, improve methods of assessing community needs, and elevate loan originations over loan purchases.

CRA regulations have remained nearly unchanged since they were last modernized in 1994. Over the last 16 years, however, the financial landscape has changed significantly, with substantial consolidation of the financial sector, entry of non-bank financial institutions into provision of products and services traditionally offered by banks, and radically different business models for financial services providers. Recognizing the need for CRA modernization, the Federal Deposit Insurance Corporation (FDIC), Federal Reserve Board, Office of the Comptroller of the Currency (OCC), and Office of Thrift Supervision (OTS) held hearings across the country in the summer of 2010 to collect public comments to inform updated CRA regulations. Woodstock Institute, along with dozens of community organizations and interested individuals, testified at the hearings with practical recommendations that would bring CRA in line with modern banking practices and improve the ability of the regulators to use CRA to engender meaningful community investment. Disappointingly, little progress has been made in the three years since the hearings and the proposed changes to the Q&As do not address many of the concerns raised in the public testimony.

About Woodstock Institute

Woodstock Institute is a leading nonprofit research and policy organization in the areas of fair lending, wealth creation, and financial systems reform. Woodstock Institute works locally and nationally to create a financial system in which lower-wealth persons and communities of color can safely borrow, save, and build wealth so that they can achieve economic security and community prosperity. Its key tools include applied research, policy development, coalition building, and technical assistance. Based on 40 years of research, policy development, advocacy, and technical assistance in the field of community reinvestment, Woodstock Institute is in a unique position to provide substantive recommendations to improve the CRA.

Improvements to guidance on community development lending and services

We strongly support the proposed language on additional ways to determine whether community development recipients are low- and moderate-income (LMI). The expanded definition of LMI will facilitate necessary investments in services provided to recipients of public benefits programs. In addition, regulators should include participation in the following programs as proxies for LMI status: Temporary Assistance for Needy Families; Women, Infants, and Children; Supplemental Security Income; Head Start; Section 8 vouchers; and other means-tested programs.

We support the explicit consideration of nonprofit board service as a technical assistance activity that can be provided to community development organizations. This change would expand valuable expertise available to nonprofits working in community revitalization. Positive consideration of nonprofit board service should be granted only if board members actually participate actively on the board and perform services that benefit low- and moderate-income people.

We also strongly support the new proposed language that addresses the quantitative consideration given to certain types of community development investments. Financial institutions may invest or lend to an organization that invests those funds and uses the income, or a portion of the income for community development. Prior to this proposed Q&A, banks may have received CRA credit for the full dollar amount of the funds, even though a small portion was used for community development. Clarifying that banks will receive only positive consideration for the amount of invested funds used for community development prevents banks from artificially inflating CRA performance.

Finally, we strongly support the proposed new Q&A that clarifies that community development lending is always a factor that is considered in an institution's CRA rating. The OCC previously issued guidance stating that community development lending performance could only have a positive or neutral impact on the lending test assessment. This fails to hold banks accountable for poor or nonexistent practices in lending that primarily benefits low- and moderate-income communities. We are pleased that regulators explicitly state in the proposed Q&A that "an institution's record of making community development loans may have a positive, neutral, or negative impact on the institution's lending test rating." Poor community development lending products and practices should always be reflected negatively on a CRA exam.

Elevating community development lending and investments

Woodstock Institute appreciates the desire of the regulators to affirm the importance of community development lending and investments. As stated above, Woodstock agrees that community development must be accorded a high level of importance, but we have concerns that the language in the proposed Q&As could potentially elevate community development lending at the expense of the retail lending test.

The proposed Q&As change how community development lending is weighted on the CRA lending test. The proposed language states that "strong performance in retail lending may compensate for weak performance in community development lending, and conversely, strong community development lending may compensate for weak retail lending performance." This language must be deleted. Retail lending is the predominant part of the lending test, and it is unlikely that strong performance on community development lending can or should compensate for weak performance on retail lending. The proposed language could have the unintended consequence of decreasing the level of bank retail lending.

A more effective method for affirming the importance of community development lending would be to create a separate community development test. The community development test would incorporate community development lending and investments for all activities that primarily benefit low- and moderate-income communities. The important work of community development lending should be evaluated on its own merits, not as a replacement for retail lending.

Modernizing assessment areas

The intent of current Q&As is to allow community development lending outside of an institutions' assessment areas, as long as community development needs are adequately met within a bank's assessment areas.[1] This can promote community development work in rural or small metro areas where

[1] See current Q&As §___.12(h)—6.

there are a limited number of bank branches. Due to comments from financial institutions indicating confusion around what is meant by "adequately addressing" community development needs within their assessment areas, the proposed Q&As re-state that section to say that community development activities outside of an institution's assessment areas "may not be conducted in lieu of, or to the detriment of, activities in the institution's assessment areas."

This proposed change is an improvement over existing language and may promote increases in lending and investment to rural areas and smaller metropolitan areas. A more substantial overhaul of how banks' assessment areas are defined would promote more effective community development activities in underserved communities.

Currently, CRA regulations require only banks to serve low-income communities "in which the bank has its main office, branches, and deposit-taking ATMs."[2] While this model of assessing geographies where banks have community obligations may have been relevant in the past, it no longer reflects how banks do business today. A growing number of banks primarily conduct their business through the internet or through a network of brokers. A credit card bank may be headquartered in Delaware and have lines of credit available throughout the country, but its assessment area would cover only Delaware. As a result, banks do not have community obligations in areas where they conduct a substantial amount of transactions.

Financial activity occurring outside of assessment areas may have deleterious effects on the services offered to low-income communities and communities of color. Research from Woodstock Institute and six other organizations found that, in 2007, CRA-covered financial institutions behaved differently inside and outside of their assessment areas. In all seven metropolitan areas in the study, CRA-regulated banks made a higher percentage of high-cost loans when lending outside of their assessment areas than when lending within assessment areas. In five of the metropolitan areas examined, higher-cost loans originated in low- and moderate-income tracts by CRA-covered depositories lending outside of their assessment areas exceeded the higher-cost rates from nondepository mortgage lenders.[3] This suggests that while CRA has been effective at promoting responsible lending to low- and moderate-income communities, significant gaps are created by the antiquated branch-based definition of assessment areas that could affect the economic opportunity of low- and moderate-income consumers.

Updating the definition of CRA assessment areas to ensure that banks are meeting the credit and banking needs of their true market area would be a more effective mechanism for promoting investment in underserved communities than the semantic changes contained in the proposed Interagency Q&As. Assessment areas should be defined as any state, metropolitan area, or rural county where an institution maintains retail offices or is represented by an agent or has at least a 0.5 percent market share in housing-related loans, securities, insurance, or any other financial instrument designated as CRA-eligible for the purposes of establishing an assessment area.

Any changes to community development lending and investment obligations would be strengthened by requiring enhanced data disclosure on these activities. Currently, lenders report the total dollar amount

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[2] "Assessment area delineation." *Federal Register* 12 §228.41 (8 July 2004).
[3] Paying More for the American Dream III: Promoting Responsible Lending to Lower-Income Communities and Communities of Color. Woodstock Institute et al, 2010. Web.

and number of community development loans. Community development lending and investments should be reported at the census tract or, at minimum, the county level so that it is possible to analyze how well communities are being served. This would also allow the public to gauge how well any changes to the Q&As promote community development loans and investments to underserved communities and propose additional modifications as necessary.

Improving the services test and surveying community needs

The service test needs to be significantly reformed. Currently, the only quantitative measure in the service test is the number of bank branches in low- and moderate-income communities. The mere existence of a branch in a low- and moderate-income tract does not serve as an adequate proxy for providing services to low- and moderate-income individuals. Regulators must assess data on the individuals accessing bank branches and the services provided to them. Specifically, regulators should examine critical variables such as census tract location, information on account holders, number of new accounts opened, age of accounts, average annual account balances, and percent of bank income generated by fees. Similarly, prepaid cards are increasingly being offered as a checking account alternative, particularly to low- and moderate-income consumers. Data on prepaid card holders, transaction volumes, and fee income should be examined by regulators as well. These data should be made publicly available, similar to the Home Mortgage Disclosure Act, so that the public can identify and hold banks accountable for gaps in access to bank services.

Finally, the goal of the Community Reinvestment Act is to ensure that banks meet the credit and financial services needs of low- and moderate-income communities where they do business. There is no objective measure of what those credit and financial services needs are, however. Regulators should establish an interagency survey of financial services needs and require banks to publicly release their community investment plans. The public would be able to use these two elements to measure whether banks are living up to their community investment goals and the needs of the communities they serve.

Conclusion

Many of the reforms in the proposed Q&A would modestly improve the implementation of CRA, but more comprehensive changes are necessary to assessment areas, community development lending, the services test, and transparent ways of measuring community needs. We urge prompt and comprehensive reform to the CRA regulations.

Sincerely,

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