MICHIGAN COMMUNITY CAPITAL
investing in places where people come first

August 5, 2022

Mr. James P. Sheesley, Assistant Executive Secretary
Attention: Comments RIN 3064-AF81
Federal Deposit Insurance Corporation
550 17th Street NW
Washington, DC 20429

Mr. Eric Hanna, President & CEO
Michigan Community Capital
Magnet Lending Corporation
507 South Grand Avenue
Lansing, MI 48933

RE: Community Reinvestment Act, Docket ID OCC-2022-0002

Dear Mr. Sheesley:

Michigan Community Capital (MCC) appreciates the opportunity to comment on Docket ID OCC-2022-0002, the "Notice of Proposed Rulemaking (NPR) on Reforming the Community Reinvestment Act Regulatory Framework." MCC strongly supports the Community Reinvestment Act (CRA) while also acknowledging that there are aspects of the law and its administration that could be improved.

MCC is a 501(c)(3) tax-exempt public charity, a Community Development Entity (eligible allocatee of New Market Tax Credits) and its subsidiary, Magnet Lending Corporation, is a certified community development financial institution (CDFI) which lends and invests in order to benefit low-income and low-wealth communities across Michigan. Since our 2004 inception, we have invested more than $1 billion in urban and rural Michigan communities. This financing has helped to create or maintain over 4,000 jobs, construct or rehabilitate over 1.75 million square feet of community development real estate and create over 900 affordable housing units. Without CRA-qualified investments, MCC would not be able to drive our mission of investing in low- to moderate-income communities, creating jobs and creating low- and middle-income housing.

Please note that some but not all of our comments overlap with comments provided by Opportunity Finance Network, the national association for CDFI's.

CDFIs and the Community Reinvestment Act

Over the past 45 years, CRA has helped bring affordable housing, small businesses, jobs, and banking services to underserved communities. Part of the 1977 Housing and Community Development Act, the CRA is a landmark civil rights accomplishment, rooted — along with the Voting Rights and Fair Housing Acts — in the Civil Rights Act of 1964. Together, these laws have taken us closer to being a nation that lives up to its stated founding principles of equality for all.

Inspired by the civil rights movement, the very first CDFIs set out to prove that access to affordable, responsible credit can transform a community. There are now more than 1,400 CDFIs certified by the Department of Treasury's Community Development Financial Institutions (CDFI) Fund with more than $222 billion in total assets.[1] With cumulative loan loss rates of less than 1 percent, CDFIs lend prudently and productively in exactly the low- and moderate-income (LMI) communities that are the focus of CRA.[2]

Banks often partner with CDFIs to enter new markets that were previously ignored or "redlined." These communities have reaped benefits, not only from the growth in CRA-motivated capital, but also from the partnerships between banks and CDFIs. Both banks and CDFIs have realized that working in partnership can enhance both institutions' effectiveness in reaching underserved markets. In fact, CRA-motivated bank debt has been a key driver in the expansion of community development loan funds - data from Opportunity Finance Network (OFN) members show that borrowed funds from banks grew from $775 million in 2005 to $4.7 billion in 2020.[3]

Proposed Reforms to the Community Reinvestment Act Regulations

Michigan Community Capital is pleased to provide comments on the proposed revisions to the Community Reinvestment Act. Our comments reflect a commitment to a community development finance industry in which banks and CDFIs are important partners in expanding access to capital and credit.

The proposed reforms represent a "once in a generation" opportunity to shape the community development finance ecosystem. These significant new regulations update the CRA in critical ways and bring the regulations more in line with the current financial services marketplace. We are especially pleased to see that the regulators have adopted a joint regulatory framework, avoiding the risk of regulatory arbitrage with banks "flipping" their charters from one agency to another to find the most advantageous regulations. However, the proposal also misses opportunities to further extend the impact of CRA.

Reforms to the regulatory framework of the Community Reinvestment Act (CRA) must advance the primary purpose of the statute: assuring that banks provide appropriate access to capital and credit to their communities. Many of the proposed reforms to the CRA regulatory framework are positive reforms:

- *Continued recognition of the critical role community development financial institutions (CDFIs) play in helping banks meet their CRA obligations.* MCC is pleased to see that the regulators acknowledge the value of CDFIs as partners to drive credit and capital to underserved markets. CDFIs have demonstrated that when you remove access to credit as a systemic barrier, communities in decline can begin to come back, and even thrive. Today, CDFIs provide financing

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[1] CDFI Fund FY 2019 Annual Certification Report database.
[2] Id at 2.
[3] OFN Annual Member Survey Data.

where it is needed most— to marginalized people throughout the United States, including in persistently poor inner cities and rural small towns.

However, while the Notice of Proposed Rulemaking makes important strides in codifying the partnerships between CDFIs and banks, there are several areas where the language should be strengthened and improved to ensure there is no ambiguity about how CDFIs should be treated. We are strongly urging the Agencies to retain and emphasize this language on page 93 that places ALL CDFIs on an equal footing with Minority Depository Institutions (MDIs) and Low Income Credit Unions (LICUs) as qualifying for CRA consideration regardless of their location relative to an examined bank's assessment area.

In particular, the agencies must affirm that **"All activities with Treasury Department-certified CDFIs would be eligible CRA activities. Specifically, lending, investment, and service activities by any bank undertaken in connection with a Treasury Department-certified CDFI, at the time of the activity, would be presumed to qualify for CRA credit given these organizations would need to meet specific criteria to prove that they have a mission of promoting community development and provide financial products and services to low- or moderate-income individuals and communities."**

The agencies propose two other changes to the regulation involving Minority Depository Institutions (MDIs), Women-Owned Depository Institutions (WDIs), Low Income Credit Unions (LICUs), and CDFIs. The regulations should ensure that CDFIs are explicitly included in key provisions:

i. The regulation should explicitly include "CDFI" in language related to consideration for "investments, loan participations, and other ventures undertaken by any bank, including by MDIs and WDIs, in cooperation with other MDIs, other WDIs, or LICUs".[4] CDFI banks are the only set of CRA-regulated depositories that are annually certified as primarily serving LMI communities, and LICU's and CDFI credit unions do not have perfectly overlapping customer base or service areas. **It is critical that the regulation explicitly include CDFIs in this category to clarify that activities undertaken with ALL CDFI types will receive positive consideration.**

   The agencies also seek feedback on whether activities undertaken by an MDI or WDI to promote its own sustainability and profitability should qualify for consideration but does not include CDFI banks in this section.[5] There should be clear language explicitly including CDFI banks within this category of mission-driven lenders.

[4]Page 92 of NPR.
[5]Page 93 of NPR.

- *Including CDFIs on the proposed list of Impact Review Factors.* In addition to the proposal's explicit recognition of activities carried out in conjunction with CDFIs, many aspects of the impact review point to the benefit of partnering with CDFIs and their deep market knowledge. Impact Review Factors would capture activities that are particularly impactful and responsive to community credit needs.

- *Updating assessment areas.* MCC applauds the long-awaited revision to assessment areas to reflect shifts in the financial services industry away from deposit-based banking. The proposed rule would provide banks with consideration for activities outside their deposit-based areas, and to align examinations and accountability more closely with financial institutions' actual markets and lending.

- *Expansion of activities considered in reviews.* The inclusion of additional activities in the lending test, including automobile lending, online lending, and credit card lending**,** more accurately captures financial institutions' provision of service to consumers and helps ensure that all activity meets the needs of communities.

- *A Community Development Financing Test.* A Community Development Financing Test that incorporates both qualitative assessment and qualitative review recognizes the important role that community development lending and investment play in banks' ability to meet the needs of their markets and reflects the need for a flexible and tailored approach to assessing those activities. However, key aspects of the community development test must be improved and are noted in the sections below.

- *Expanded consideration of community development activities conducted outside of bank assessment areas.* Bank branch locations do not always align with the neighborhoods most in need of investment, and this is particularly true for the communities many CDFIs serve. The proposed geographic flexibility can help bring community development capital to more neighborhoods. This expansion will be especially useful for rural communities where banks have limited assessment areas.

- *A shift toward data-driven evaluations*. Grounding CRA review in data will improve understanding of gaps in lending, investment, and services. The collection of additional data including information about deposits, race and ethnicity of borrowers, lending to small businesses will also enhance regulators' bank partners and the public's understanding of the full scope of bank lending in underserved communities. Data must, as the proposal notes, be complemented by more flexible qualitative reviews to foster innovation and adjust to local markets and partners.

Areas of Improvement Needed to Strengthen the Proposed Rule

While many areas of the proposal are steps in the right direction, there are key areas of the Notice of Proposed Rulemaking (NPR) that must be improved:

- *Encourage Banks to Assist CDFI's with the Asset Transformation Function.* CDFI Loan funds, apart from regulated CDFI Banks and Credit Unions, comprise a large portion of certified CDFI's. Those organizations have a different capital structure. As a consequence of the lack of ability to sell stock or take deposits, they struggle to perform the "borrow short, lend long" Asset Transformation Function that depository institutions perform. In revising the CRA, regulators should consider how to encourage banks to facilitate this function when lending to CDFI's. As noted in the Carsey 2012 report, the lack of asset transformation function likely contributes to lower enterprise leverage among non-depository CDFI's and meaningfully higher cost products for low-income borrowers.

  MCC urges the agencies to examine the cost of funds loaned to CDFI's versus the cost of bank funds used to make those loans and to encourage banks to provide the lowest overall practical and prudent cost of funds to CDFI's so as not to result in higher interest rates to lower income borrowers…the opposite of the intended purpose of the CRA.

- *Increase the Rigor and Weighting of the Community Development Financing Test.* The proposed rule's weighting of retail test performance and community development test performance could have unintended consequences of undermining the importance of community development in CRA. As currently structured, Community Development performance would not affect most large banks' overall CRA rating because retail test performance weighs heavier (60%) than Community Development performance (40%). The proposed weight of 40% given to community development does not reflect its importance to community reinvestment.

  Under the new ratings system, very few banks would be able to achieve an Outstanding rating. As the National Housing Conference and other stakeholders note – if an Outstanding retail test rating is not achievable, a bank will receive an overall Satisfactory rating even if its Community Development test score is Needs to Improve as long as its retail test score is Low Satisfactory – a standard that nearly all banks are likely to meet or exceed.[6] Banks could dramatically scale back their community development activities without impacting their overall rating – which could have devastating consequences on the community development finance ecosystem and the CDFI industry.

  MCC recommends rebalancing the retail test performance and community development test performance so that each would account for 50% of a bank's rating. This would ensure that community development performance is still an integral part of a bank's CRA rating.

- *Improve Consideration of Equity Investments in Community Development Financing Test.* While MCC appreciates the agencies' consideration of community development financing activities as an integral part of CRA, it may deemphasize proven tools including the New Markets Tax Credit and the Low-Income Housing Tax Credit. Under the new rule, large banks will have a "Community Development Financing test" that combines many of the activities previously evaluated as community development lending and community development investments. We at MCC are

[6] NHC blog post

concerned that this combined evaluation of community development loans, investments, and services will cause a shift in banks CRA activities away from more complex, time consuming but impactful activities like making equity investments in or grants to CDFIs, in favor of making more community development loans.

We recommend requiring a minimum amount of community development finance activity be in the form of equity investments in order for a bank to achieve a passing rating. We further recommend that a portion of this equity be not tied to the purchase of tax credits. Providing equity only for the benefit of purchasing tax credits significantly limits banks' appetite to work with CDFI's, CDE's and community driven organization to meet the diverse needs of LMI households. Banks should be required to demonstrate a creative and responsive mix of equity investments, as meeting equity tests only through tax credit purchases allows them to make assumptions about a community's needs along with developers instead of actually working with the community on creative solutions.

- *Strengthen the Community Development Services Test.* The community development services test, while accounting for 10% of the overall rating, is too weak to encourage effective development of community development services. In order for services to be a meaningful contribution to the overall community development financing strategy of a bank, the services test must evaluate and give credit for useful and impactful activities that are responsive to the needs of a bank's community. We at MCC, echo the below recommendations, presented by OFN's network members, to strengthen the community development services test:
    - Add grant contributions to CDFIs and nonprofits with a community development purpose as a measure on the CD Services Test. This is an opportunity to not just emphasize grant contributions to CDFIs but also motivate banks to provide operating support for local community development organizations. The agencies could distinguish between operating grants (which would be eligible on the CD Services Test) and programmatic grants (which would be eligible on the CD Finance Test).
    - Shift the CD Services Test to meaningfully evaluate the responsiveness of CD activities. The CD Services Test could look at the mix of community development financing options provided by a bank to determine how responsive a bank's products are to the community. To ensure "responsiveness" is a meaningful component of the overall exam, the CD

      Services Test could be increased from 10% of the overall CD rating to 15% or 20%. For example, a bank that provides financial support to an MDI could get this activity counted as an Impact Review Factor regardless of the type of financial support provided, whereas the CD Services Test would consider it particularly responsive if the financial support was an equity investment in the MDI, as opposed to a certificate of deposit.
- *Provide Greater Clarity on Impact Review Factors.* The CD Financing Test does propose including grant contributions as an Impact Review Factor, yet it remains unclear how great of an emphasis

Impact Review Factors will have in a bank's final rating. Certain activities should be considered especially impactful and responsive. The agencies should also consider providing multipliers or additional credit for activities undertaken with certified CDFIs – with an emphasis on providing more credit for grants and equity investments.

- *Reconsider New Bank Size Thresholds that Could Reduce Community Development Financing.* Another area of concern is the agencies' proposal to raise the bank size threshold and the potential impact that could have on community development financing, especially in smaller or rural markets. The NPR would set new thresholds for small and intermediate banks. Under the proposal, small banks are defined as those with assets of up to $600 million and Intermediate Banks (ISBs) are those with assets of at least $600 million but less than $2 billion. Large Banks are those with assets of at least $2 billion. These changes would reclassify 779 banks that are currently ISBs as small banks, meaning they would no longer have community development finance responsibilities.

  Reducing the number of banks that have community development responsibilities could have a negative impact on the flow of capital to CDFIs – particularly CDFIs in rural markets that already have access to less CRA-motivated bank capital. As provided by OFN, member data shows that only about 30% of borrowed funds for rural CDFIs come from CRA-motivated banks as compared to about 50% for urban CDFIs. Smaller banks are often important partners for these CDFIs. Reducing the number of banks that have community development obligations would disrupt the flow of capital to those CDFIs that have the specialized knowledge and deep community relationships to help increase access to responsible finance in markets with limited options.

Conclusion

MCC appreciates the opportunity to comment on potential changes to the CRA regulatory framework. The proposed rule makes important strides in updating this critical rule's ability to drive capital and investments into the communities that need it most. With a few additional tweaks to the proposal, the new rule would be closer to reflecting the modernized financial services landscape and better addressing the credit needs of underserved communities. MCC looks forward to continuing to partner with the regulatory agencies to refine the proposal.

Sincerely,

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Eric Hanna, President and CEO
Michigan Community Capital