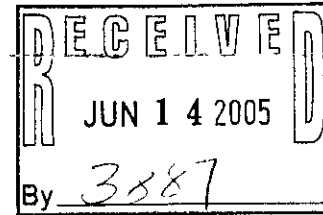




Independent Bankers Association of New York State

125 State Street
Albany, NY 12207
Phone 518 436 4646
Fax 518 436 4648

June 6, 2005



Mr. Robert E. Feldman, Executive Secretary
Attention Comments
Federal Deposit Insurance Corporation
550 17th Street, NW
Washington, DC 20429

Attention. RIN 3064-AC89

Re: Community Reinvestment Act Regulations

The Independent Bankers Association of New York State, Inc , which exclusively represents the interest of community banks located throughout New York State submits this comment letter in support of the May 10, 2005 comment letter submitted by the Independent Community Bankers of America on the joint proposal by the Federal Reserve, FDIC and OCC to revise the Community Reinvestment Act (CRA) rules to address regulatory burden.

As consolidation continues to dominate the financial services industry, regulators should continue to examine the eligibility thresholds. Banks in excess of a billion dollars but less than \$2 billion in assets in New York State engage in an extremely competitive marketplace. Efforts should be made to retain and eliminate regulatory burden for such larger community banks. The continued thrust of regulatory burden relief should be to encourage a competitive marketplace and to level the playing field for community banks which are unable to apply the economies and efficiencies of mega-banks when dealing with compliance issues from regulators.

The opportunity to comment on the pending regulations is greatly appreciated.

Sincerely,

William Y. Crowell, III
Executive Director



U.S. DEPARTMENT OF THE TREASURY
FEDERAL RESERVE SYSTEM
WASHINGTON, DC 20512
ATTENTION: COMMUNITY BANKS
REGULATORY AFFAIRS
DIVISION

May 10, 2005

Robert E. Feldman, Executive Secretary
Attention: Comments
Federal Deposit Insurance Corporation
550 17th Street, NW
Washington, DC 20429
Attention: RIN 3064-AC89

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

Jennifer J. Johnson, Secretary
Board of Governors of the
Federal Reserve System
20th Street and Constitution Avenue, NW
Washington, DC 20551
Attention: Docket No. R-1225

Re Community Reinvestment Act Regulations

Dear Sir or Madam:

The Independent Community Bankers of America (ICBA)¹ appreciates the opportunity to comment on the joint proposal by the Federal Reserve, FDIC and

¹ The Independent Community Bankers of America represents the largest constituency of community banks of all sizes and charter types in the nation, and is dedicated exclusively to representing the interests of the community banking industry. ICBA aggregates the power of its members to provide a voice for community banking interests in Washington, resources to enhance community bank education and marketability, and profitability options to help community banks compete in an ever-changing marketplace.

With nearly 5,000 members, representing more than 17,000 locations nationwide and employing over 260,000 Americans, ICBA members hold more than \$631 billion in insured deposits, \$778 billion in assets and more than \$493 billion in loans to consumers, small businesses and the agricultural community. For more information, visit ICBA's website at

OCC to revise their existing Community Reinvestment Act (CRA) rules to alleviate regulatory burden without weakening CRA. The proposal would increase the asset size limit for eligibility for the small bank streamlined examination to \$1 billion. To address concerns raised by critics of previous proposals, the agencies would add a new community development test for "intermediate small banks" (those between \$250 million and \$1 billion in assets). Finally, to provide added flexibility, the proposal would expand the definition of community development to include activities in "underserved" rural areas and designated disaster areas.

Summary of ICBA Position

To reduce unnecessary regulatory burden, the ICBA supports a simple streamlined CRA exam for all banks under \$1 billion without regard to holding company status. Although we would prefer a straightforward increase in the threshold, the ICBA also supports a community development criterion for mid-tier banks between \$250 million and \$1 billion, including expanded recognition for activities that benefit rural residents and communities.

Eligibility for the Streamlined CRA Examination Should be Expanded.

As long as community banks are subject to the Community Reinvestment Act, the ICBA strongly supports a tiered CRA regulatory system with a streamlined examination for community banks to minimize regulatory and paperwork burden. To reduce unnecessary regulatory burden, the ICBA strongly supports an increase in the asset size limit for eligibility for the streamlined examination and elimination of the holding company size qualification as an unnecessary complication. Extending the streamlined exam to more community banks would foster the goals of the 1995 CRA reform—to insure the regulations emphasize performance over process and eliminate unnecessary regulatory burden. To be equitable, banks should be evaluated against their peers, not in the same context as banks hundreds of times their size that stretch from coast to coast. Assessing the CRA performance of a \$500 million bank or a \$1 billion bank using the same criteria as for a \$500 billion bank, as current procedures do, is inappropriate.

Community banks, as integral parts of their communities, rely on vibrant communities to thrive. Expanding eligibility for the streamlined exam will not change the way community banks do business or lessen their resolve to reinvest in their communities. In fact, by alleviating unnecessary paperwork and examination burden, it will allow community banks to reallocate and redirect both human and financial resources to their communities and customers.

The Community Development Criterion for Mid-Tier Banks Must Be Flexible. The ICBA supports including a community development criterion—that considers lending, investments and services—in the exam for mid-tier banks between \$250 million and \$1 billion in assets. The greater flexibility of such a community development criterion, as compared to the current, restrictive investment

test, will allow community banks to establish more effective community development programs that focus efforts locally, based on market needs and opportunities and the bank's strategic strengths. "Qualified investments" that target only the requisite low- and moderate-income residents and areas are often not available in many community banks' assessment areas. As a result, the investment test forces many community banks to divert resources to make "qualified investments" that may have little direct impact in their own communities.

The ICBA also supports a definition of community development that gives credit for activities that benefit rural residents and communities even if not targeted solely to low- and moderate-income individuals or areas. Such a definition recognizes the unique challenges of rural areas, where inadequate public infrastructure is a significant roadblock to economic development and where demographic patterns often make it difficult to segregate low- and moderate-income geographies.

Expanding Eligibility for the Streamlined Exam Would Provide Needed Regulatory Burden Relief. CRA compliance examination costs place an unfair burden on "large" community banks. An ICBA/Grant Thornton study entitled, "*The High Cost of Community Bank CRA Compliance: Comparison of 'Large' and 'Small' Community Banks*" reveals that CRA compliance costs can more than double when community banks exceed \$250 million in assets and are not examined using the streamlined procedures. A survey of community banks showed the mean employee cost attributable to CRA is 36.5% higher at large community banks compared to small community banks. In each of two case studies—one contrasting costs for a bank that grew from "small" to "large" bank status, and one contrasting costs for "small" and "large" banks owned by the same holding company—CRA compliance costs were four or more times greater for large community banks than for small ones. The study showed that large bank investment test is also a cost burden for large community banks. Ninety-two percent find the market for CRA investment opportunities "competitive" or "highly competitive" and 69% say such investments are "not readily available." Half the respondents report giving yield concessions to make CRA-qualified investments.

Summary of Specific Comments

- ICBA strongly supports increasing the eligibility threshold for the streamlined small bank CRA exam to \$1 billion while eliminating the separate holding company qualification.
- A simple increase in the "small bank" threshold to \$1 billion would be preferable, but a new community development assessment for mid-tier banks between \$250 million and \$1 billion ("intermediate small banks") is acceptable.

- As an alternative, the ICBA urges the agencies to consider a simple increase in the size limit for the small bank streamlined exam to \$500 million since regulatory burden disproportionately impacts small banks and their communities the most, and applying the community development assessment to banks between \$500 million and \$1 billion in assets.
- The ICBA supports indexing of the thresholds, and recommends growth in industry assets be used as the benchmark.
- A separate community development factor added to the existing small-bank evaluation criteria would be preferable to a separate test for intermediate small banks.
- Since the CRA statute and the current regulatory evaluations focus on lending, the streamlined lending test should be given greater weight than the community development test.
- Examination procedures for intermediate small banks should be published for public comment prior to implementation.
- ICBA applauds the agencies' proposal to expand the definition of community development, since the current focus on low- and moderate-income factors do not work well in rural communities.
- The FDIC's August 2004 proposal to define community development to include activities that generally benefit rural areas or residents would be easier to apply and less burdensome.
- Any definition of rural should incorporate several alternative elements, including rural counties designated by the Census Bureau, nonmetropolitan counties designated by the Department of Agriculture and, within metropolitan counties, census tracts designated as rural by a government authority.
- To define "underserved rural" areas, the banking agencies should incorporate several alternative factors, including communities with declining population or low- and moderate-income as defined by HUD, and rural areas targeted by federal or state government programs for economic development.
- ICBA also supports including activities that benefit designated disaster areas in the definition of "community development."

Background of the Proposal

Recognizing the burdens of CRA examinations and the demographic changes in the industry since the streamlined small-bank exam was first adopted in 1995, in

February 2004, the banking agencies jointly proposed increasing the threshold for the streamlined small-bank CRA exam to \$500 million, without regard to holding company assets. Commenters on the proposal split, with community activists strongly opposed and the ICBA and the banking industry strongly in favor of the proposal. After extensive discussions, the agencies were unable to reach consensus.

Last July, in an unusual step, the OTS independently increased the threshold for the streamlined CRA examination for thrifts to \$1 billion without regard to holding company size. The OTS rule does not include a separate evaluation of community development activities as part of the streamlined exam. After the OCC announced its rule, the Federal Reserve and OCC withdrew their proposals to increase the small bank threshold to \$500 million.

In August 2004, the FDIC issued a separate proposal to set the small bank limit at \$1 billion, eliminate the holding company size limit, and add a new community development criterion to the small bank test for banks between \$250 million and \$1 billion in assets. The FDIC also proposed to expand the definition of activities that qualify as "community development" activities under CRA by including activities that generally benefit residents of a rural community.

The ICBA strongly supported the FDIC proposal. The FDIC received approximately 11,500 comments on its August 2004 proposal, including those from many ICBA members who supported the proposal. However, the proposal also drew a great deal of criticism from community activists. As a result, it appeared that there might be a stalemate on CRA, with only the OTS electing the higher threshold for streamlined small bank CRA exams.

Then, in February, the Federal Reserve, OCC and FDIC reached consensus on a revised proposal (the current one) that builds on the earlier proposals and the many comments received by the agencies. According to the agencies, the goal of the latest proposal is to "balance the objective of providing meaningful regulatory relief for additional community banks with the objective of preserving and encouraging meaningful CRA activities by those same banks."²

The Current Proposal

Increased Small Bank Threshold. The major change in the current CRA proposal would be to increase the size of banks eligible for the small bank from \$250 million in assets to \$1 billion in assets. As with previous CRA proposals, the separate holding company qualification would be eliminated. The current proposal also would provide a mechanism to allow the agencies to adjust the threshold to account for inflation.

² 70 *Federal Register*, p. 12150, March 11, 2005.

The agencies are proposing this step to address the serious problem of regulatory burden, a point strongly emphasized by the ICBA. Banks with less than \$1 billion in assets would no longer be required to collect and report data on small business, small farm and community development loans. The agencies believe that the elimination of the data collection requirements is perhaps the most significant burden reduction element of the proposal.

ICBA Comments. In ICBA's view, the agencies' proposal to increase the threshold is a good step that is likely to help reduce the staggering regulatory burden experienced by the nation's community banks. With the many demographic changes across the banking industry in the 10 years since the streamlined CRA exam was first implemented, including industry consolidation and growth of the largest banks, the \$1 billion asset-level is an appropriate benchmark for a tiered CRA regulatory system.

Generally, community banks with less than \$1 billion in assets must serve all income segments their market areas or they would not survive. Compliance with the investment, service and lending tests, as well as the data collection requirements, that apply to large banks under the CRA is a drain on resources, especially for banks with less than \$1 billion in assets.

Indexing the Threshold. The agencies also propose indexing the threshold for the streamlined CRA exam based on changes to the Consumer Price Index (CPI). Currently, the Federal Reserve uses the CPI to adjust the threshold of banks exempt from HMDA data collection and reporting requirements. The ICBA supports indexation of the threshold, and believes that the CPI is a logical benchmark.

However, the ICBA recommends that the agencies give serious consideration to using growth in industry assets as the benchmark for indexation instead. In order to keep pace with developments in the banking industry, it would be more logical to use overall growth in industry assets to measure increases in the size of banks eligible for the small bank streamlined CRA exam

New Community Development Test for Intermediate Small Banks. Under the proposal, instead of the current large bank three-part test (lending, investments and services), intermediate small banks would be evaluated using the small bank retail-lending test and a new community development test of equal weight. The second test would evaluate: (a) the number and amount of the bank's community development loans; (b) the number and amount of qualified investments; (c) the extent to which the bank provides community development services; and, (d) the bank's responsiveness through such activities to community development lending, investment and services needs. An intermediate small bank would have to receive a minimal rating of "satisfactory" on **both** the lending test and the community development test to receive an overall "satisfactory" CRA rating. Intermediate small

banks would no longer be subject to the three separate "lending," "investment" and "services" tests that apply to large banks.

The agencies believe that this new test will give intermediate small banks greater flexibility to provide community development services in their own communities. For example, banks will no longer be required to make investments to satisfy CRA requirements that do not directly benefit or only marginally benefit the local community. Instead, the new test is designed to let community banks undertake more effective community development activities based on the bank's business strategy and capacity as well as the opportunities and needs of its community—whether lending, investment or service. However, the agencies stress that while the new test will permit banks to receive credit for activities that are not necessarily innovative, complex or new, the agencies do not intend to allow banks to simply ignore one or more categories of community development.³

ICBA Comments The ICBA would prefer to see a simple increase in the CRA small bank threshold to \$1 billion, without the addition of a separate community development review. However, we also believe that the creation of a middle tier of "intermediate small banks" is an acceptable compromise that should still help alleviate burden for intermediate small banks without weakening CRA. The ICBA agrees with the agencies' assessment that the combined evaluation of community development lending, investments and services, instead of discrete reviews and evaluations for each category, will provide added flexibility.

Community Development Test for Intermediate Small Banks. The ICBA especially supports the flexibility in the proposal that will allow each community bank to allocate resources in the most appropriate way to serve its own community, without having to identify and invest in activities that may benefit the larger geographic area but that do not benefit the bank's own community. This has been a particular problem for banks under \$1 billion that are currently subject to the large bank review. Combining the factors of community development lending, investments, and services into a single test will also be a more effective evaluation of community development performance. The proposed community development test should mesh with the overall strategic goals of most community banks to serve their communities and will better reflect what the bank is actually doing to support the needs of its own community.

Alternative Threshold for the Community Development Test. Although the ICBA strongly supports a simple increase in the threshold for the streamlined small bank CRA exam to \$1 billion, and although we accept the creation of a mid-tier "intermediate small bank category," the ICBA also suggests that the agencies consider an alternative. As has been frequently noted, smaller community banks are suffering under regulatory burden, to the point where many are merging or selling to larger institutions. Taking the community bank out of the community does not further

³ *Federal Register*, volume 70, no. 47, Friday, March 11, 2005, p. 12151.

the goals of the CRA. The ICBA believes that an appropriate compromise would be a straightforward increase in the threshold for the **current** streamlined CRA examination to \$500 million (as the agencies proposed last year), with a community development assessment for banks between \$500 million and \$1 billion. Smaller institutions are most affected by regulatory burden, and a simple increase in the threshold to \$500 million would help the community banks that need it most.

Lending Should be Given Priority. Instead of creating a separate, equally weighted community development test, the ICBA would prefer adding a criterion for community development activities to the existing factors in the streamlined CRA exam. The ICBA supported such a step in the FDIC's August 2004 proposal and continues to believe that an additional criterion rather than a separate test would be preferable.

Fundamentally, banking is the business of accepting deposits and making loans. The CRA exam should be an evaluation of a bank's lending activities to ensure that deposits from the community are being returned to the community through loans. Therefore, the ICBA believes that the lending elements of CRA should be given priority. A bank's overall lending performance is a better barometer of its community involvement, and should be weighted more heavily. The CRA statute specifically states that the agencies should evaluate a bank's efforts for meeting the *credit* needs of its community.⁴ In fact, in the current CRA ratings matrices used for large banks, lending activities are given greater weight. Therefore, lending should be given more weight than the community development test. Based on the large bank rating matrix, and keeping with the Congressional mandate, the lending test should at least factor two times more than the separate community development test.

Development of Examination Procedures for Intermediate Small Banks. A critical element to the success of the proposal in reducing regulatory burden will be how examiners in the field apply the final rule. An advantage to both the existing rule and the proposal is the flexibility permitted for banks in determining appropriate activities. However, by the same token, that very flexibility can lead to subjectivity. Bankers report that some examiners exhibit a tendency to give credit to an activity as long as it is on an "approved" list that has passed muster or been deemed acceptable by regional headquarters but dissuade bankers from making community development investments in their own communities if the investment has not already been evaluated by the regional office or agency headquarters.⁵ While this makes it easier for an examiner to make a determination, it also undermines the basic premise of the CRA and detracts from the concept of "performance context."

⁴ 12 USC 2903(a)(1).

⁵ For example, bankers have been told that an "appropriate" investment would be the purchase of housing bonds issued by one of the GSEs instead of local investments not already approved by agency headquarters that would have to be independently evaluated by the examiner.

Perhaps more important, it undermines the ability of community bankers to invest in qualifying local projects

In addition, the proposal would permit examiners to use performance context to give credit to investments that reflect an ongoing commitment by the bank, even though the investment was considered during the previous CRA evaluation. The ICBA believes this is an important step, since it will allow credit for ongoing programs that benefit the community. Banks must invest time and effort to make these investments, and if the community is continuing to benefit, then the effort should continue to be recognized. To do otherwise discourages bank efforts for ongoing commitments to their communities. The ICBA also encourages examiners to consider activities that take place between examinations, such as a community development loan that is funded and then paid off between exams.

Examiner training is especially important because the community development test is designed to be a blending of community development lending, investments and services—not a separate evaluation like the current large bank tests. Examiner training is critical to ensure that examiners do not take the elements of the community development test outlined in the proposal and turn it into three separate assessments. Doing so would defeat the purpose of the change and would undermine the design of the new community development test.

To ensure these goals are accomplished, new examination procedures and guidelines will be critical. When initial examination procedures on the new community development criteria have been drafted, the ICBA strongly recommends that the draft procedures be published to allow interested members of the public to comment. The ICBA also strongly encourages the agencies to conduct outreach meetings to educate examiners and bankers on the new requirements once they are finalized. Ideally, these training sessions will be for bankers and examiners simultaneously so that everyone hears the same message.

Burden Reduction for Intermediate Small Banks. The agencies indicate that perhaps the most significant element of burden reduction in the proposal will be eliminating data collection and reporting requirements for intermediate small banks.⁶ Currently, large banks must collect and report data on small business, small farm and community development loans.

The ICBA agrees with the agencies' assessment that this is, perhaps, the most significant burden reduction element in the proposal. Training staff, data entry, and ensuring the integrity of data is a very time consuming and burdensome process that some community banks characterize as "onerous."

However, even though the proposal would eliminate formal data collection and reporting for banks under \$1 billion, it will not eliminate the burden altogether.

⁶ 70 *Federal Register*, p. 12151, March 11, 2005.

Whenever an activity is subject to regulatory scrutiny as is CRA performance, banks are compelled to institute some type of internal monitoring system to ensure compliance. Therefore, while an internal monitoring system may not be required by regulatory mandate, community banks will still have to monitor data. Even banks currently eligible for the streamlined CRA exam (those under \$250 million in assets) must have some type of monitoring system to evaluate their own compliance. Many intermediate small banks already have systems in place for the current data collection requirements and are likely to continue using them. Therefore, it is not clear how significantly elimination of this requirement will reduce burden, but it is a step that the ICBA strongly supports.⁷

“Community Development”

The proposal would expand the definition of “community development” for all banks. The current definition focuses on activities that benefit low- and moderate-income individuals and areas. Because many rural areas do not include census tracts that can be easily designated low- or moderate-income, the expanded definition would include (1) affordable housing in underserved rural areas and (2) revitalization and stabilization activities in underserved rural areas. However, under the proposal, examiners would give significant weight to factors such as the extent to which low- and moderate-income individuals benefit from a particular activity. The definition also would be expanded to include activities that benefit disaster areas. An area would qualify if it has received official designation as a disaster area.

ICBA Comments. The ICBA applauds the agencies’ efforts to expand the current definition of community development. The existing definition fails to provide sufficient recognition for community services to individuals in rural areas or designated disaster areas. Overall, the ICBA believes that investments that benefit a local rural community, including investments that benefit the local municipality, school district or that help improve local infrastructure, should qualify. Activities that help to stabilize and revitalize communities are important, a point often made by community groups, and should receive credit under CRA.

Community Development Needs in Rural Areas. Recognizing the need for development activities that benefit rural communities,⁸ the August 2004 FDIC proposal would have expanded the definition of “community development” to include activities that generally benefit rural areas or residents, an approach the ICBA strongly supported.⁹ The FDIC proposal would have implemented a simple solution to the problem, while also recognizing that activities that generally benefit a rural

⁷ It is worth noting that an informal survey of ICBA bankers found that none had ever been asked to produce this data by any organization other than the banking agencies.

⁸ See, e.g., *Rural Depopulation: What Does it Mean for the Future Economic Health of Rural Areas and the Community Banks that Support Them?* Jeffrey Walser and John Anderlik, FDIC Banking Review, volume 16, no. 3, p. 57.

⁹ ICBA Comment Letter, October 20, 2004.

community will have broader reaching benefits that support the underlying premise of the CRA. However, because many activists complained this would allow banks to receive CRA credit for *any* activities that benefit a rural community, including activities that might only benefit high income individuals, the agencies revised the proposal to focus on "underserved" rural areas, especially affordable housing.

~~Rural communities across the United States are struggling with unique~~ community and economic development needs and challenges. In fact, the plight of our nation's rural communities was one rationale advanced by the Federal Reserve for retreating from the February 2004 proposed CRA regulatory relief. The proposed new definition of "community development" begins to tackle this problem by including activities that benefit rural residents.

The National Association of Development Organizations Research Foundation found that inadequate public infrastructure is viewed as the most significant roadblock to economic development in small town and rural America.¹⁰ The remote nature of rural regions and weak local educational systems rounded out the top three greatest hurdles to job creation and growth in smaller communities. Limited access to venture capital and business development financing also ranked as significant problems.

Community banks in rural areas are often called upon to provide funding for crucial local projects, such as municipal infrastructure or community improvements, or to help create jobs by attracting businesses to their communities and providing small business credit. Because of population distribution patterns, rural areas are often not neatly segregated into low-, moderate- and high-income areas. It is frequently difficult to isolate needed community development activities in rural areas so that they are focused solely on low- and moderate-income individuals or geographies. It is important to recognize that community development activities in rural areas should not be ineligible for CRA credit, as they are now, because they do not benefit *only* low- and moderate-income individuals.

It is important to grant CRA credit to banks in rural areas for supporting needed economic or infrastructure development such as job creation to employ rural individuals or provide better paying jobs in rural areas where average incomes are lower than in metropolitan areas. Even more important, the CRA rules should encourage infrastructure development, something that is often challenging in rural areas due to lower tax bases and lower property values. Activities as diverse as funding a local water project or school construction, rehabilitating a Main Street retail district, or offering a special program to bring the unbanked into the financial mainstream, should qualify.

¹⁰ "EForum Results: The Pulse of Small Town and Rural America," NADO Research Foundation, August 2004, page 6.

A problem with applying the existing community development definition to rural communities is that, unlike the inner city, rural communities are not as neatly separated into low- and moderate-income tracts. For example, according to a presentation by the Federal Reserve,¹¹ 51% of banks with under \$250 million in assets have no low- or moderate-income tracts in their assessment areas (as the FDIC recognized in the August 2004 proposal). The ICBA believes that the ~~problems associated with using the low- and moderate-income approach for rural areas~~ have produced the difficulties under the existing CRA rule for rural banks and their communities. Correcting that problem demands a solution that does not rely solely on traditional analysis but looks more generally at rural communities. In addition, the current CRA definitions of low- and moderate-income do not work for rural areas because they are much too low, particularly since they are measured against statewide **nonmetropolitan** median income, which is generally lower to start with than the statewide median or the metropolitan area median.

The ICBA continues to believe that the FDIC's August 2004 proposal without reference to "underserved" is the most straightforward and least burdensome resolution to the problem that rural areas are not as easily identified as low- or moderate-income. However, it might be possible to achieve a simple definition for "underserved rural" communities that can be easily applied by bankers, examiners and other interested parties.

Defining Rural. First, "rural" must be defined. The ICBA believes that several alternative factors must be used to identify an area as "rural" for the purposes of CRA. One factor should be population density, but it should not be the sole defining factor. In fact, to coordinate with existing programs designed to benefit rural communities, including underserved rural communities, a broad definition of rural for CRA purposes is needed.

Census Bureau Definition. A starting factor for defining an area as "rural" is population density, and the most logical application would be the existing definition established by the Census Bureau. However, according to a July 2004 article on *Defining Rural America* by the Federal Reserve Bank of Kansas City, most analysts find the Census Bureau definition (places with fewer than 2,500 residents) too restrictive.¹² Therefore, more is needed.

Department of Agriculture Designation. The two major housing government-sponsored enterprises (GSEs), Fannie Mae and Freddie Mac, provide special housing loans designed to benefit rural communities. For example, Fannie Mae has partnered with the Rural Housing Service of the Department of Agriculture (RHS) to offer several special loan products for rural residents. According to Fannie Mae,

¹¹ Briefing, Federal Reserve offices, April 21, 2005.

¹² *Defining 'Rural' America*, Jason Henderson and Stephan Weiler, *The Main Street Economist*, Center for the Study of Rural America, Federal Reserve Bank of Kansas City, July 2004, p. 2.

these products are designed to "provide low and moderate-income rural residents with better access to credit and decent housing." Fannie Mae also entered into a partnership with RHS on a special pilot project to offer affordable multifamily rental housing for low- and moderate-income families. Similarly, Freddie Mac works with RHS on projects designed to reach underserved markets and to "help more low-income rural borrowers achieve the dream of homeownership." Like Fannie Mae, Freddie Mac partners with the Department of Agriculture's Section 502 Single-Family Leveraged Second Loan Program, designed to meet the needs of low-income rural borrowers

To coordinate with these efforts by the housing GSEs, the ICBA recommends that the CRA definition of "rural" include the Department of Agriculture designation of "nonmetropolitan."¹³ It is an already-established and readily available definition that lenders know and understand and it is widely used by Fannie Mae and Freddie Mac for their affordable housing programs. Therefore, if a county has been designated by the Department of Agriculture as "non-metropolitan," it should qualify as "rural" for CRA purposes.

A Third Alternative Factor for Identifying Rural Areas. Counties designated as "metropolitan" frequently include sections that most people would also consider "rural." According to the Federal Reserve Bank of Kansas City, "the designation of nonmetro counties as rural has been less than ideal because of the diversity in local assets and economic performance."¹⁴ Therefore, the ICBA recommends that the definition of rural be further refined to reach areas within metropolitan counties that can properly be considered rural. Therefore, if any government entity has designated a portion of a "metropolitan" county as "rural," that segment of the county should also satisfy the definition of "rural" for CRA.

In summary, the CRA definition of rural should include counties designated by the Census Bureau as rural, counties designated by the Department of Agriculture as "non-metropolitan" and, within "metropolitan" counties, census tracts designated as rural by a government authority.

¹³ Under the Department of Agriculture's definitions of "metropolitan" and "non-metropolitan," 1,090 counties in the United States are metropolitan and 2,052 counties are non-metropolitan. Although the Department of Agriculture designates communities as metropolitan and non-metropolitan, it should be simple to draft a definition that incorporates the Department of Agriculture's "non-metropolitan" definition as "rural" for CRA purposes.

¹⁴ Henderson and Weiler, *op cit.*, p. 2.

Factors to Define "Underserved Rural." The agencies also requested comments on how to define an "underserved" rural area. As with the definition of rural, the ICBA believes that incorporation of existing governmental approaches may provide a solution. However, as with "rural," alternative factors will need to be used to define a rural community as "underserved." To be successful in addressing the reinvestment and infrastructure needs of rural areas, the definition of underserved must not be too narrow.

Because many community banks operate on a county perspective, and because data on census tracts within counties is not always readily accessible, the ICBA believes that an "underserved" assessment should be made using a countywide approach. A countywide approach would be less burdensome. ICBA also believes that a county definition is more realistic because sparse population in some areas may inappropriately skew data. Community bankers with experience serving rural communities also report that it is more difficult to target markets to census tracts, since marketing to the county is less expensive, more practical and ultimately less burdensome.

Population Level. During a recent symposium,¹⁵ the Federal Home Loan Bank of Des Moines reported the results of a recent study¹⁶ that identified certain weaknesses faced by rural communities, including declining populations, difficulty retaining educated residents and lack of employment opportunities. The study also found that, contrary to traditional beliefs, agriculture is no longer a major economic driver in the vast majority of rural counties, and that greater flexibility and coordination is needed among government programs to help strengthen the viability of America's rural areas. Counties classified as "completely rural" experienced the most significant population decline or stagnation over the last decade. Rural areas were also characterized by a higher rate of poverty levels.

Therefore, to begin to address the definition of "underserved" rural area for CRA, the ICBA recommends that the definition include counties that have experienced a population decline.

Established Affordable Housing Goals. In addition to population decline, a second alternative factor for defining a rural area as "underserved" would be to incorporate reference to income levels established for existing affordable housing goals. In late 2004, HUD established new housing goals for Fannie Mae and Freddie Mac that included goals for mortgage purchases in rural areas and underserved areas.

For HUD, the Federal Housing Enterprises Financial Safety and Soundness Act of 1992 defines a low-income borrower as at or below 80% of area median

¹⁵ *Capitalizing on Rural America, A Policy Forum*, held in Washington on April 26, 2005, hosted by Senators Chuck Grassley (R-IA) and Tom Harkin (D-IA).

¹⁶ *Capitalizing on Rural America: Crafting a Competitive Future*, SRI International.

income, while the current CRA rule defines a low-income borrower as at or below 50% of area median income. Similarly, moderate income is statutorily defined for the GSE affordable housing goals as at or below 100% of median area income, while the CRA defines moderate income as between 50% and 80% of median area income.

Last fall, when HUD issued the GSE affordable housing goals, it was constrained by the governing statute from taking steps to reconcile the affordable housing goals definition of low- and moderate-income areas with those established by the banking agencies for CRA purposes.¹⁷ However, the ICBA strongly believes that it would be appropriate to reconcile these definitions, a step that the banking agencies should take by revising the CRA definitions to match those established for HUD and the housing GSEs. The ICBA also believes that the income levels established by HUD are the appropriate benchmarks. Federal Reserve analysts found that redefining low- and moderate-income levels for rural communities using this approach would greatly benefit rural communities.

Additional Factors Finally, there are a number of additional federal programs designed to provide economic development initiatives for areas across the United States without regard to median income. These areas can be easily identified by bankers and examiners and therefore are less burdensome to apply. For example, the federal government has designated "empowerment zones" designed to attract capital and investment. In addition, various states have developed programs designed to assist certain communities. As the states are closer to local problems, they may be better positioned to assess economic distress areas within their borders. The ICBA believes that areas designated by the federal or a state government as economically distressed should also be included within the definition of "underserved" under CRA.

In summary, the ICBA believes that the definition of "underserved rural areas" should include several alternative factors: (1) rural communities that have experienced a decline in population; (2) rural areas identified as "underserved" using low- and moderate income levels as defined by HUD for the affordable housing goals; *and* (3) any additional rural areas targeted by federal or state government programs for economic development.

Discriminatory Activities

The final proposed revision to the CRA rules would clarify that activities that are deemed discriminatory, e.g., violations of requirements such as Truth-in-Lending or Equal Credit Opportunity, would detract from a bank's CRA rating. The ICBA does not view this as a substantial change from existing examination procedures.

¹⁷ 69 *Federal Register*, p. 63630, November 11, 2004. When it adopted the affordable housing goals, HUD addressed the issue of reconciling the affordable housing goals for the GSEs with CRA.

However, while the ICBA does not object to this change, we also believe that it is more appropriate to use compliance examinations and fair lending reviews, which are better designed for this purpose, to identify and stop abusive lending practices.

The ICBA also urges the agencies to offer better guidance than merely listing certain regulations and suggesting that a violation of one of these regulations could lead to a downgrade in the bank's CRA rating. A bank could inadvertently have a technical violation of one of these regulations without engaging in any abusive or deceptive practice. More specifics about the kind of violations that could affect a bank's CRA rating are clearly needed, such as through an interagency Q&A. Insufficient guidance leaves too much room for uneven interpretation and enforcement by examiners.

And, although it might be appropriate for the CRA examination team to consider violations brought to their attention by another examiner within the same agency, referrals from other outside sources should be carefully assessed to ensure reliability. Moreover, any referrals that might be used to downgrade a bank's CRA rating should only be considered if the issue is final and not subject to pending discussions or investigation, and the bank should have had an opportunity to defend its actions. Whenever a CRA examiner considers these issues, the matter should be fully discussed with bank management at the start of the CRA review to put the bank on notice and allow it to address problems or raise any related points that should be considered.

Conclusion

To reduce regulatory burden, the ICBA strongly supports the agencies' proposal to increase the threshold for eligibility for the streamlined small-bank CRA exam to \$1 billion, without regard to holding company size. Although the ICBA would prefer a simple increase to the existing threshold, we accept the implementation of a community development assessment for mid-tier intermediate small banks between \$250 million to \$1 billion. However, we also encourage the agencies to consider a simple increase for eligibility for the current streamlined exam to \$500 million, with a community development assessment for intermediate small banks between \$500 million and \$1 billion in assets. The ICBA also supports indexation of the thresholds, preferably using industry growth in assets as the benchmark.

The ICBA agrees that the proposed community development assessment will be more flexible than the existing three separate large bank tests if properly implemented and applied by examiners. It also will let community banks undertake activities that benefit their local communities instead of making investments that do not directly or only minimally benefit the local area. More important, the revised community development assessment lets community banks capitalize on their strengths. Instead of a separate community development test, though, the ICBA

urges the agencies to consider adding a community development criterion to the existing streamlined exam factors, as proposed by the FDIC in August 2004, especially since the focus of CRA statute is a community's credit needs. In any event, the streamlined lending test should be given greater weight than the community development test.

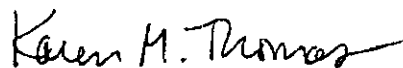
The ICBA supports an expansion of the definition of community development activities to include activities that benefit rural communities. Existing definitions focused solely on low- and moderate-income individuals or census tracts tend to undermine the purposes of CRA in rural communities by diverting funds out of the community. Because of the special development challenges faced by so many rural communities, the ICBA continues to believe that activities that generally benefit a rural community should qualify for CRA credit. However, in the alternative, existing governmental definitions established by the Census Bureau, HUD and the Department of Agriculture can be used to identify qualified underserved rural areas. ICBA also agrees it is appropriate to expand the definition to include activities that benefit designated disaster areas.

To be certain that bankers and examiners understand the revisions and how they are to be applied, the ICBA strongly encourages the agencies to publish revised examination procedures for comment, and we look forward to working with the agencies on developing such procedures. The ICBA also recommends the agencies hold outreach meetings and training to help bankers and examiners understand the requirements.

Overall, the proposal will reduce regulatory burden for community banks without weakening CRA and allow community banks to work to their strengths and engage in activities that benefit the communities they serve.

Thank you for the opportunity to comment. If you have any questions or need any additional information, please contact the undersigned or Robert Rowe, ICBA regulatory counsel, by telephone at 202-659-8111 or by e-mail at
or

Sincerely,



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