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On behalf of the
Community Development Bankers Association and CDFI Coalition

Before the Federal Financial Institutions Examination Council (FFIEC)
Hearing on Proposed Revisions to the Community Reinvestment Act Regulations
Arlington, Virginia
July 19, 2010

I thank the members of the Federal Financial Institutions Examination Council (FFIEC) for inviting me here today to discuss proposed revisions to the regulations governing the Community Reinvestment Act (CRA). My name is Jeannine Jacokes. I am the Chief Executive Officer of the Community Development Bankers Association (CDBA). I also serve as Board Chairperson of the CDFI Coalition. In addition, I also serve as Chief Executive of Partners for the Common Good (PCG), a national nonprofit loan fund that is a Community Development Financial Institution (CDFI).

CDBA is the national trade association of the community development bank sector. We are the voice and champion of banks and thrifts with a mission of serving low and moderate income communities (LMI). All of CDBA's members have been certified by the U.S. Department of Treasury as CDFIs, meaning at least 60% of their total activities are targeted to LMI communities.

The CDFI Coalition is the united national voice of community development financial institutions (CDFIs) and those that support CDFIs across all sectors of the industry, including CDFI banks, credit unions, loan funds, venture capital funds, and microloan funds. Nationwide, over 850 CDFIs serve economically distressed communities by providing credit, capital and financial services that are often unavailable from mainstream financial institutions. CDFIs have loaned and invested billions in our nation's most distressed communities.

In the 30-plus years since its enactment, CRA has spurred systemic change in the manner in which mainstream banks and thrifts serve LMI communities. It is likely trillions of dollars of credit and investment have been made in communities across the nation that otherwise would be credit starved. This has resulted in economic revitalization of these communities, and a better life for their residents. Unfortunately, much of the good work of CDFIs and their partners has been undone by the recent economic crisis. CDFIs are needed more than ever to help these communities come back—and they need the investment encouraged by CRA to leverage CDFI expertise and dollars.

CRA's effectiveness is directly linked to vigorous and consistent implementation. Despite efforts of the regulatory agencies to coordinate CRA implementation, there remains a persistent differential in implementation across the agencies – as well as across the regional offices of individual regulators. Over the past three decades, the regulatory agencies have gone through cycles of strong to weak enforcement of CRA – which is highly problematic for communities. CRA is a critical component of national economic policy and security. We need consistently enforced implementation if CRA is to contribute to the well being of LMI communities and their residents.

Over the past two-plus years, CRA has been under unfair assault by those who wish to shift the blame for the financial meltdown from Wall Street to low income neighborhoods and people. The truth, however, stands in direct contrast to those assertions. Defaults on subprime lending are widely recognized as the one of the most significant underlying causes of the financial meltdown. Research by the Federal Reserve Bank of San Francisco found that loans issued in CA by banks subject to CRA were half as likely to end up in foreclosure as loans issued by independent mortgage companies not covered by CRA. A 2008 analysis by the Board of Governors of the Federal Reserve System further found that only 6 percent of all higher-priced loans in 2006 (peak of the subprime originations) were made by CRA-covered institutions or their affiliates to lower-income borrowers or neighborhoods in their assessment areas. A 2010 analysis by the University of North Carolina's Center for Community Capital found that mortgage borrowers obtaining loans through special lending programs (including CRA) targeted to low- and moderate-income (LMI) purchasers were estimated to be 70% less likely to default on their loans than borrowers with subprime loans.

The bottom line is – CRA is essential to the health of our county's LMI communities, and banks do quality lending under CRA. From that starting point, we need to look forward and identify how CRA can become a more effective tool to: (1) promote direct lending, investments and services in LMI communities; and (2) forge partnerships with CDFIs to reach deeper into under served communities. Many of the witnesses today will focus their comments on the former. Thus, my remarks today will focus on the latter -- how CRA can support the critical work of mission focused CDFIs.

I. Investments in and Partnerships with CDFIs

CRA is the back bone of the CDFI industry's strategy to engage mainstream banks and thrifts in the work we do. Mainstream banks support our lending by providing deposits and loans that we use for relending, to borrowers that mainstream banks cannot reach as effectively as CDFIs. Mainstream banks also provide CDFIs with equity in the form of grants and as shareholders. Without CRA, the CDFI industry today would be a fraction of its current size and the scale of its lending and impact correspondingly reduced. This investment by mainstream banks in CDFIs has been consistently successful and, in the case of debt, repaid according to its terms. Working with CDFIs has been a win-win strategy for mainstream banks because it provides a way to reach hard-to-serve market niches and support innovation in the community development sector. Any revisions to CRA need to focus on supporting and encouraging CDFI partnerships.

Mainstream banks are also needed as partners with CDFIs on the transaction level. The CDFIs are often the gap financiers, with mainstream banks providing a significant portion of debt on projects. Without CRA, many of these deals would never happen because CDFIs individually and as an industry are not big enough to address all community development needs alone. Conversely, the on-the-ground and programmatic knowledge of CDFIs, as well as our ability to attract government and philanthropic funds, is a critical complement to the funds and expertise mainstream banks bring to these transactions. Thus, a strong CRA is needed to both engage mainstream banks and help CDFIs grow and do more in their communities.

- Put CDFIs on Equal Footing: All financial support provided to CDFIs should be explicitly eligible for CRA consideration. Within Interagency guidance materials, investments and deposits in minority- and women-owned banks and thrifts, and low income credit unions are explicitly listed as eligible CRA activities without regard to the geography were these institutions work. We applaud the regulatory agencies for recognizing the important contributions of these financial institutions. The entire CDFI field needs to be on equal footing and our important work recognized.

- Rewarding Effort and Impact: CRA should reward banks that provide concessionary pricing, longer term support, or other favorable terms on deposits and investments in and loans to CDFIs. Similarly, banks that work with CDFIs to develop innovative products and services for LMI markets should be recognized more explicitly and strongly in the evaluation process. While the regulations state that "innovative or complex" activities will receive consideration, implementation has not been adequate. CRA implementation is currently strongly focused on measuring the number and dollar amount of transactions. This focus has the unintended consequence of creating disincentives for mainstream banks to: (1) provide longer term financing, which would reduce liquidity risk and asset-liability management challenges for CDFIs with demand for long term loans, but only short term money to lend; or (2) engage in transactions that are highly impactful, but may take years to put together and involve multiple financing sources. Implementation of CRA should be amended to reward mainstream banks for providing support to CDFIs in manner that enables them to meet customer needs in a financially sustainable manner.

- Eliminate Footprint Mismatch: All financial support provided to CDFIs by banks should be explicitly eligible for CRA consideration regardless of whether a CDFI is located in and/or serves the same service area as its mainstream bank investor(s). As currently implemented, most banks get: (1) minimal CRA consideration for CDFI related activity outside of their designated assessment areas; and (2) limited consideration for such activities even within assessment areas unless the assessment area receives a full-scope exam. This treatment dissuades mainstream banks from supporting CDFIs that are not located directly in their markets and/or principally serve the same geography as the bank. The resultant mismatch means missed opportunities to multiply banks' ability to deliver credit and investments to underserved areas, particularly those whose needs exceed the capacity of local institutions subject to CRA.

- <u>Assessment Areas Should Reflect Real Markets</u>: CRA should cover all broad geographies in which a bank does significant business. In particular, industrial loan companies and wholesale, investment, credit card, or internet based banks should not have local assessment areas. They should be expected to meet community development needs on a national basis, which is more reflective of their actual markets. Given some of the practical limitations on financial institutions that do not have a retail presence in many of the places that are part of their actual markets, regulators should explicitly recognize and give significant weight to investments in and/or partnerships with CDFIs.

- <u>CRA Support for CDFI Liquidity Enhancement Strategies</u>: Over the past 24 months, the liquidity crisis within the broader financial services sector has exacerbated and highlighted the long term challenges of the CDFI industry in managing portfolio liquidity. Unlike the traditional financial services industry, the CDFI field lacks the sufficient institutional infrastructure to manage portfolio liquidity through loan syndications, secondary market sales, and other mechanisms. Efforts to sell securities backed by pools of CDFI originated loans to mainstream banks seeking CRA credit have encountered challenges. For example, examiners have had difficulty in determining how or if to give CRA credit when a bank purchases an interest in a loan pool that may include loans both within and outside of a bank's assessment area. Or, a regulator may give one bank "credit" for a specific loan within a pool, but deny another bank credit for the same loan. As purchasers of the pool, both banks have a fractional interest in all loans and should be given CRA consideration in proportion to their investment in the entire pool. While the regulations permit proportional treatment, implementation both across and within the agencies is inconsistent and often confusing. We urge the regulatory agencies to improve their examiner training and work toward greater consistency.

II. Tool to Help CDFIs Subject to CRA Advance Mission

Among the 862 certified CDFIs nationwide there are 62 CDFI banks and thrifts that are both subject to CRA examinations and are often recipients of support from other banks seeking CRA consideration. Within this group, 45% have "Outstanding" CRA ratings and 55% have "Satisfactory" ratings. This compares to mainstream banks where 16% have an "Outstanding" rating and 80% have a "Satisfactory" rating. CDFI banks are mission driven institutions with a strong focus on their low income communities.

CRA implementation needs to be amended to be more efficient and effective in helping CDFI banks to (1) maximize their service and the dollars deployed into LMI communities; and (2) support innovation and impact. We strongly encourage greater integration of CRA requirements with the U.S. Treasury Department's Community Development Financial Institutions Fund (CDFI Fund)'s Programs. We believe the regulatory agencies and LMI communities could benefit from adopting some of the highly effective strategies used by the CDFI Fund to promote access to capital (discussed below). In addition, we urge incorporation of the following changes to CRA:

- <u>Serving New Underserved Communities</u>: The purpose of the 1977 CRA statute is to ensure that credit-worthy borrowers in LMI communities have access to credit as measured by the amount of money flowing into a community. As such, CRA appropriately focuses on whether banks make loans within their designated assessment areas. While CDFI banks seek to maximize their activities within their target markets, we urge for CRA consideration of loans made by CDFI banks within low income census tracts that are outside of a formally designated assessment area. Given their missions, CDFI banks often get demand from borrowers in underserved communities outside of their immediate target markets. Many of these areas are equally unserved. In some cases, these communities may eventually become part of a CDFI bank's formal service area. While such activities are unlikely to constitute a significant portion of a portfolio until they become part of a formal market or assessment area, the activities are often critically important to communities very much in need of responsible finance. By definition as mission based institutions, CDFI banks are highly committed to low income communities (e.g. at least 60% of all of their activities must be targeted to underserved communities). CDFI banks urge the regulators to enable them to receive CRA consideration for all loans in low income census tracts regardless of whether those tracts are currently in the bank's assessment area.

- <u>Community Development Loans</u>: The current Community Development Loan definition is: (1) too narrow to capture the breadth of activities that CDFI banks engage in that create benefits for the community; and (2) highly burdensome to document. For example, the prohibition against classifying loans to businesses with total revenues of $1 million or greater as CRA eligible should be eliminated or modified to take into consideration impact. Within the LMI communities such larger businesses can generate significant numbers of jobs for residents and create other benefits. We encourage the agencies to eliminate definitions that limit eligibility on high impact activities. We also encourage the agencies to streamline and reduce the documentation burden of demonstrating that a loan has "primary purpose" of community development. In the case of markets served by CDFI banks, nearly all investment is good and generates economic activity. It may be more appropriate to develop a list of loan purposes that are inappropriate or harmful to the community (e.g. pawn shops, liquor stores, pay day loans) and prohibit CRA consideration for such activities. This approach is successfully used by the CDFI Fund in its New Market Tax Credit Program (NMTC).

- Rewarding Innovation & Impact: CRA implementation is too heavily focused on quantitative measures of performance at the expense of activities that are innovative and often more beneficial to the community. The regulatory agencies need to balance quantitative with qualitative measures. As noted above, while the regulations state that "innovative or complex" activities will receive consideration, implementation has not been adequate. The CDFI Fund's Bank Enterprise Award (BEA) Program provides a good illustration of a system that is effective at balancing both. Using a system of "priority factors" and "weighted values," the BEA gives greater consideration in its ranking and award calculation process to activities that are more difficult or costly than others, but which create greater community benefits. Regulators should amend CRA implementation to more effectively and clearly reward banks that engage in innovative and/or highly impactful CRA activities.

- Expand Service Test Definition: Regulators should amend the Service Test to give CRA consideration to small banks providing retail products and services – particularly to engage the un- and under-banked into the economic mainstream. Currently, small banks only get CRA credit under the Service Test for their volunteer and grant making activities. Providing alternatives to pay day lenders, pawn shops, and predatory providers of financial services is of critical national importance. Small community based banks are the first line of defense in curbing abusive practices. While all small banks should not be required to provide or report such services, if they undertake these activities, they should be given Service Test credit for them. The BEA Program also provides a model for how to incent banks to engage in developing targeted financial services for underserved populations.

- Support Deposit Raising Strategies: When CRA was enacted it was intended to stop bank "red lining" -- raising deposits in LMI communities without lending back. Today regulators appropriately look at the relationship between deposits raised from LMI communities and the amount reinvested back. This ratio, however, does not give adequate consideration to institutions that raise a multiple of deposits outside of LMI census tracts that are "imported" in to support community development in LMI areas. Operating in places with modest discretionary income and insufficient means to raise deposits, an integral part of the strategy of most CDFI banks is to raise deposits from civic-minded, philanthropic, and socially-motivated individuals and institutions (as well as CRA motivated mainstream banks) to meet the demand for credit in LMI communities. As such, in the case of CDFI banks, we urge that the Service Test be revised to give CRA credit for importing deposits into LMI tracts.

III. Making CRA More Effective in All Communities

In the three decades since its creation, CRA has been the bedrock of ensuring LMI neighborhoods and people are not shut out of the economic mainstream. The responsibility for promoting an inclusive prosperity by ensuring access to capital, however, should not be borne only by CDFIs and mainstream banks. When CRA was created, the bulk of financial services were delivered through traditional retail branches of locally controlled banks. The financial services industry has changed dramatically with the rise of trillion dollar money center banks, elimination of barriers that prevented non-bank entities from offering a spectrum of financial products and services, and the growing size and influence of capital markets. While the industry has changed, CRA has not kept up.

CRA needs to be updated to reflect the current flow of capital to more diverse sectors of the financial service industry. In the interests of reflecting these broader trends and leveling the playing field, all quarters of the financial services sector (e.g. insurance companies, investment banks, mortgage companies) should share responsibility and have an obligation to ensure that credit worthy people and places are not left out of the economic mainstream.

We believe Congress needs to revisit the statute's focus on CRA evaluations solely in the context of banks, with an enforcement mechanism geared to those seeking to expand by acquiring a bank or branch. Since the statute was enacted, we have learned a great deal about how access to credit is the life blood of economic opportunity to all Americans. Regardless of whether a financial institution is considering expanding or not and whether it has a bank charter or not, it should be obligated serve the entire community of credit worthy customers within its market area.

However, regulators also have a role. As an increasing number of non-bank financial services institutions come under the bank holding company umbrella, we urge bank regulators to maximize CRA's reach within the current statute. CRA examinations need to look both at the activities of the bank and its affiliates to get a true picture of its performance in serving communities. Banks should be given positive consideration for activities undertaken by affiliates that create positive benefits; conversely, if a non-bank affiliate is engaged in delivering products and services that create negative impacts it should be considered in the overall context of the examination.

Finally, we urge that the regulatory agencies enhance their understanding and expertise in community development. Community development needs, deals and partnerships are often complex. Better training is needed for examiners to enable them to understand credit needs of low income communities, effective strategies for reaching under served markets, community development finance products, and the operating constraints of CDFI banks. Given the variability among community development transactions, examiners must have the authority to make qualitative judgments. Enhanced training, coupled with clear but flexible guidelines, will improve CRA evaluations and consistency within and among regulators.

Since its enactment, CRA has spurred systemic change in the manner in which banks and thrifts serve LMI communities. CDFIs have become critical players in serving low income markets. But, we cannot do it alone. Working in local communities, we have all seen that when CRA is vigorously and creatively enforced, communities win. We strongly urge the regulatory agencies to adopt the recommendations of the CDFI industry.

Thank you for the opportunity to express these views and work with you to better serve our communities.