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Before

Public Hearing on

Community Reinvestment Act Regulation Hearings

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Good morning, I am Terri Ludwig, Executive Vice President and Chief Operating Officer of Enterprise Community Partners. Enterprise is a national nonprofit organization. We create opportunity for low- and moderate-income people through fit, affordable housing in diverse, thriving communities. Enterprise provides financing and expertise to community-based organizations for affordable housing development and other community revitalization activities throughout the U.S. For more than 25 years, Enterprise has invested over $10 billion to create more than 270,000 affordable homes and strengthen hundreds of communities across the country.

To begin, I would like to thank you all for showing the leadership and initiative to convene these hearings to ask thoughtful questions about how to improve the regulatory implementation of the Community Reinvestment Act (CRA.) My career in investment banking and nonprofit leadership prior to coming to Enterprise has been intertwined with CRA. I have led nonprofits that benefited from bank investments driven by CRA and I also led the Merrill Lynch Community Development Company which was subject to CRA. I have seen how CRA made financial institutions see new lending and investment opportunities in low-and moderate-income communities and also how the CRA regulations sometimes did not work as well as intended.

Enterprise and other community developers that are testifying here today sent a joint letter in December asking that you commence a review to update the CRA regulations. As you all know, CRA is a broad statute that leaves the regulatory agencies considerable discretion to design the system to evaluate bank performance. The 1995 revisions to CRA regulations that created the "lending" "service" and "investment" tests provided a great improvement in the rigor and transparency of CRA examinations. The financial services industry has continued to evolve since then, however, and it is time to assess the whether further changes are needed to keep CRA relevant and useful. I applaud your leadership in convening these hearings and I look forward working with you to keep CRA a constructive force directing investment into low-income communities.

Currently, the community development industry faces many challenges including the problems in the larger economy that have diminished investor interest in tax credits and the declining efficacy of CRA's regulatory regime. Again, Enterprise supports your initiative to reopen the CRA regulations. There are four areas that we think are especially important: the need to create a "community development test", the importance of examiner training, recognition for green building practices and the need to rethink how assessment areas are determined and how banks get credit for activities.

Community development test:

The community development field has evolved a great deal since the "lending," "service" and "investment" tests for larger banks were created in 1995. At that time, the legislation creating Community Development Financial Institutions (CDFIs) had just passed. Thanks in part to the

CDFI statute, CRA, tax credits, and other policies, a whole industry has arisen that provides credit to low-income communities and individuals on more favorable terms than the private market alone could provide. Community Development Financial Institutions (CDFIs), community development credit unions, community development banks, loan funds, community development corporations (CDCs) and other socially-motivated investors finance affordable rental housing, economic development projects, community facilities like child care centers, and other projects that bring hope and jobs to low-income communities.

CRA, in combination with other policies mentioned above, has given financial institutions the motive and opportunity to invest in public-private partnerships with local CDCs and CDFIs, and sometimes local governments. These partnerships then invest in economic development projects, affordable housing, and other amenities that improve neighborhoods. Tax incentives like the Low Income Housing Tax Credit and the New Markets Tax Credit only work with private sector investment. Government grant programs like the Treasury's CDFI Fund and programs at the Department of Agriculture and Small Business Administration also support these activities.

Currently, evaluation of bank activities in these areas is scattered among the lending, service, and investment tests, depending on the form the investment takes. The dollar value of one loan on a supportive housing project that involved state and local government and a CDC can be dwarfed by a bank’s volume of conventional home mortgage lending in low-and moderate income neighborhoods, yet that community development loan can have a larger impact on the neighborhood. The time and complexity required by community development projects needs to be recognized by a separate test that looks at community development as an integrated whole.

This is why current regulations should be augmented with a rigorous but qualitative "community development test" that replaces the investment test. Lending, services and investments in affordable rental housing, economic development projects, community facilities like child care centers and charter schools, community loan funds, microfinance loan funds, and other community development activities in low-and moderate- income communities should qualify for this test. Equity investments in community development financial institutions and other investments in building the capacity of community developers should qualify as well. The dollar value of the activity should be considered as well as how far the institution has stretched to meet community development needs, consistent with safe and sound lending.

Effective community development starts with an assessment of the community's needs. The regulatory agencies should work together on an interagency assessment for each major metro area that replaces the assessments of community needs done by individual agencies as part of CRA exams of various financial institutions. The agencies might want to contract out this responsibility to a knowledgeable, independent third party like a research firm or an academic institution. Public input should be a crucial part of this assessment. Bank performance could then be judged against an independent third party assessment of metro demographics, economic trends and community needs. It would be a great improvement over the current system if the assessments were uniform across agencies and were used for all of the institutions in the region that were examined.

A final thought on the Community Development Test is that currently there is no real incentive for institutions to get an "outstanding" rating. The system would be more effective if there were a more powerful incentive for performance, consistent with other CRA policies. The agencies should consider giving awards for community development leadership and recognition for best practices. Perhaps the green building field offers a model to consider. Developers with exemplary building practices are recognized and certified according to the Enterprise Green Communities Criteria or the U.S Green Building Council's LEED standard. Developers actively seek these designations. A similar "race to the top" for CRA performance could really benefit low-income neighborhoods.

Examiner training:

The "community development" test should reflect qualitative judgment of how much value community development investments, services, and loans add to communities. The current system is overly focused on quantitative targets that don't reward institutions for serving their communities well with products that meet community needs. A community development test by its nature requires more qualitative judgment than creating a table of mortgage lending data. The creation of a community development test requires training of bank examiners to succeed.

Enterprise would be happy to work with our community development colleagues and the banking agencies to design a curriculum for bank examiners that reflects the lessons and complexities of our more than twenty five years of community development experience. There are difficult questions about whether particular loans or investments really meet neighborhood needs. It is not reasonable to expect safety and soundness examiners with cursory training in community development to make judgment calls about whether an institution's products and strategy meet community needs. More rigorous and thoughtful training for bank examiners will be needed to make a community development test live up to its promise.

Green building:

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Financial institutions should receive extra consideration under the "community development test" if the housing or commercial developments financed in a low- or moderate-income area are energy efficient and built according to green building standards like the Enterprise Green Communities criteria. Over the past five years, Enterprise has supported the development of over 17,000 homes built according to Enterprise's Green Communities Criteria, the first national framework for environmentally sustainable affordable homes. The Criteria were developed in collaboration with and endorsed by a number of leading environmental, energy, green building, affordable housing, and public health organizations.

In creating Green Communities, Enterprise sought to show that all affordable housing – new construction and rehabilitation, homeownership as well as rental, large urban developments and small rural projects – could be green within the budgets and capacity of the typical affordable housing developer. Enterprise has demonstrated that green affordable developments can be created for little if any higher development costs than conventional projects that do not offer the same benefits. Our extensive evaluation efforts have generated data that show we can create affordable housing that is environmentally sustainable for only marginally higher development costs – 2 percent over total development costs – and those first costs can come down with experience. Green building benefits residents living in a healthier environment and contributes to the financial viability of the projects due to measures such as energy and water efficiency that generate financial savings over time.

Enterprise's experience with Green Communities suggests that adding in an environmental overlay to CRA does not require any dilution of the low-and moderate-income focus of CRA. All lending, or investments that receive credit under CRA should serve low- and moderate-income communities and we are not suggesting that should change. What Green Communities has taught Enterprise is that green and affordable housing can be one and the same, and similar thinking should infuse the creation of a “community development test” that allows for additional consideration for green buildings that serve low- and moderate- income communities.

Assessment areas:

The concept of “assessment areas” under CRA needs to be reconsidered. One of the most difficult regulatory issues that you will grapple with is deciding where and how to give banks credit for lending, investment and services. Under the current system, banks have a strong incentive to lend and invest in the assessment areas that receive a full-scope CRA exam, and much less of an incentive to do business elsewhere. This results in some areas being "credit deserts" because they are not part of any financial institution's CRA footprint.

When CRA was passed in 1977, there was neither nationwide banking nor a community development industry. CRA encouraged banks to lend in the neighborhoods from which they took deposits. Today, in a world of nationwide banking and deposit taking and a wide array of mission-oriented community development conduits, like CDFIs, loan pools, or tax credit investment funds, it seems misguided to focus on only giving banks CRA credit where they take deposits. A better question to ask is “Is this high quality community development work that meets a need in a low- and moderate-income neighborhood?”

The agencies should consider different sorts of assessment area determinations for different sorts of financial institutions. True community banks that operate within one state should have community development responsibilities where they have branches. Larger institutions with branches in multiple states should have community development responsibilities where they have physical presence, but should also receive CRA consideration for lending and investments in nonprofit mission-oriented community development conduits like CDFIs that operate outside of their geography, as long as these institutions are meeting legitimate community development needs.

The largest financial institutions with nationwide branches pose a particular challenge. They should be evaluated on their performance in the largest metro areas where they have a physical presence, plus on a statewide basis for the balance of the those states, but they should also be scrutinized for their efforts in meeting nationwide community development challenges such as special needs housing or affordable, green development. Your recent regulatory proposal to give banks additional credit for foreclosure response activities is a good example of using CRA to meet a national community development challenge and we look forward to working with you to refine the proposal.

Limited purpose, credit card, and wholesale banks should be in a different category. They also should be evaluated on the basis of their national community development partnerships and not just on limited markets where they take deposits. Where deposits are booked is a banking law technicality. For these institutions, CRA performance should be judged more broadly in the context of their national financial presence.

Conclusion:

CRA is an unusual and powerful law whose effectiveness needs to be maintained. It is unusual because it is a broad, affirmative obligation for the private market. CRA doesn't prohibit behavior; instead it lays out a broad goal that is to be met consistent with safe and sound banking. And it has succeeded in fostering an industry that tackles tough community development challenges. As Federal Reserve Chairman Ben Bernanke observed last summer, "As the effects of the financial crisis and the resulting economic downturn have spread, there has been increased focus on preserving the gains made in low- and moderate-income communities over recent decades. Accomplishing that objective requires preserving the institutions that helped build these communities. Without strong CDFIs, attracting investments and capital to rebuild and revitalize communities would be even more difficult. Economic recovery, like economic development, is a bottom-up as well as top-down process. Through their work at the community level, CDFIs, together with other community development organizations, can help build a sustainable recovery for all of us."

Thank you for your efforts to maintain the strength and relevance of CRA. Enterprise would be pleased to work with you on these complicated and difficult issues.