

From: Peter Hainley [mailto:phainley@casaoforegon.org]
Sent: Tuesday, August 31, 2010 5:34 PM
To: Comments
Subject: Community Reinvestment Act Regulation Hearings-Docket ID OCC-2010-0011, Docket No. R-1386, RIN 3064-AD60, Docket ID OTS-2010-0019

Dear Sir/Madam:

CRA Comments

As a non-profit organization that serves predominately minority populations in rural communities throughout Oregon, I see first hand the under-investment by financial institutions in our rural communities. By reforming CRA, we can get bank investment into these rural communities leading to stronger economies and better partnerships among the rural populations and the financial institutions that serve them.

Meaningful reforms to CRA will ensure economic recovery that promotes sustainable lending to small businesses for job creation and responsible home lending. While we applaud your intentions to improve CRA, regulatory action alone is not sufficient. Congress needs to apply CRA broadly throughout the financial industry in order to maximize safe and sound lending and investment in communities.

CRA promotes care and sustainability in lending. The law requires safe and sound lending, and would have been a preventative cure to the foreclosure crisis had it covered a broader range of institutions. Research conducted by Federal Reserve economists documents that home loans made by banks in their CRA assessment areas are about half as likely to end up in foreclosure as loans issued by independent mortgage companies. In addition, CRA small business and community development lending exceeded \$1 trillion for America's neighborhoods from 1996 through 2008.

Although CRA has been instrumental in boosting lending and investing, neglect of certain parts of the regulation has meant that CRA has not realized its full potential. If CRA had been updated, the level of CRA-lending and investing would have been substantially higher. In particular, we believe that regulatory rulemaking should address the following areas:

Assessment Areas

As currently defined by the CRA regulation, assessment areas, the geographical locations covered by CRA exams, generally consist of metropolitan areas or counties that contain bank branches. However, while some banks still issue loans predominantly through branches, others make the majority of their loans through brokers and other non-branch means.

As a result of the current definition of assessment areas, the share of all home purchase loans made by banks operating in their CRA assessment areas has dropped to about 25 percent. Narrow assessment areas facilitate problematic lending practices that are not scrutinized on CRA exams. Research demonstrates that lending by institutions not covered by CRA or by banks outside of their assessment areas is more likely to be high-cost.

Currently under CRA regulations banks are not held accountable for performance outside of their largest service areas. This results in less oversight of investments made in low income communities which leaves room for suboptimal servicing on loans provided to these customers and can foster poor performance in certain places like rural counties without penalty. In order to ensure that rural areas are given adequate attention we recommend that a bank's CRA rating be based on its performance throughout its entire service area. By requiring ratings in all assessment areas, a low rating could be detected and an improvement plan required so that a given bank would be more likely to serve distressed rural areas well. We suggest CRA regulations and any revisions to the CRA statute define eligible investments in distressed "rural" areas as those rural areas defined in section 520 of the Housing Act of 1949. This definition best mirrors the rural character of the communities we serve that are most underserved by traditional financial services and capital markets.

It is important that activities undertaken by bank affiliates are considered during CRA examination and reflected in ratings since many financial services are provided to rural borrowers through affiliates of bank institutions like credit card providers. Regulations that require examination of affiliate activities are necessary. If statutory changes are made to CRA to better ensure the needs of low and moderate income borrowers in rural areas are met, we support the Community Reinvestment Modernization Act of 2009 (HR 1479) provision that amends the CRA statute by requiring banks that capture 0.5% or more of a local lending market to include that local geographic area in its assessment area, allowing for the first time rural counties to be rated, not just examined.

The Office of Thrift Supervision (OTS) is the one agency that went beyond official assessment areas on CRA exams for non-traditional thrifts, but these exams still examined only a minority of the thrifts' loans. We ask the agencies to significantly improve upon the OTS' precedent and meaningfully include the great majority of bank and thrift loans on CRA exams.

Apply the same 3 CRA performance tests to bank institutions of all sizes.

Institutions with assets up to \$1.098 billion are now considered small by CRA definition. This increased asset threshold is a recent regulatory change that has exempted additional bank institutions from two key CRA tests. In 1995 the asset threshold for banks defined as "small institution" was \$250 million or less. Small institutions are provided a streamlined CRA exam and this is troubling as larger institutions are brought into this examination category. As a result of recent regulatory changes that increased asset benchmarks, banks with assets up to \$1.098 billion are not required to take the investment or services test, just the lending test. We believe all CRA regulated financial institutions regardless of asset size should be held to the same oversight standards and required to meet all three tests on their CRA exam.

Many rural lenders are small institutions and without capturing investment or service data from these lenders in CRA examination, the communities we serve are risk pullback of bank lending to rural areas. Banks that were once considered large did have an obligation to service the distressed rural communities where we work, and we have been troubled by recent reductions in lending to low income rural businesses and projects now that these

institutions are considered "small" and are exempt from the CRA investment and services tests

Mandatory Inclusion of Mortgage Company Affiliates on CRA Exams

Under CRA, banks have the option of including their non-depository affiliates, such as mortgage companies, on CRA exams. Banks are tempted to include affiliates on CRA exams if the affiliates perform admirably, but will opt against inclusion if the affiliates are engaged in risky lending or discriminatory policies. We believe the agencies have the authority to include all non-depository affiliate lending on CRA exams to ensure that the lending affirmatively responds to credit needs in a safe and sound manner.

Include Bank Lending and Service to Minorities on CRA Exams

Given the evidence of lending disparities by race, we believe that CRA exams must explicitly examine lending and services to minority borrowers and communities. A large body of research shows that minorities received a larger percentage of subprime loans than whites, even after controlling for borrower creditworthiness and other characteristics. Overall, it is probable that considering lending and branching by race of borrower and neighborhood on CRA exams would lessen the racial disparities by encouraging banks to increase their lending and services in communities of color. Before the 1995 changes to the CRA regulation, CRA exams considered lending to minorities as an assessment factor, suggesting the agencies thought they had the authority to consider lending to minorities on CRA exams.

CRA Exam Ratings and Weights

The scale of four possible ratings does not provide meaningful distinctions in performance and has resulted in a 98 to 99 percent pass rate over the last several years. The agencies should introduce Low and High Satisfactory as possible ratings in addition to the four existing ratings. In addition, the agencies should develop better weighting systems so that routine investments like purchasing loans on the secondary market do not receive as much weight as more difficult investments such as equity investments in small businesses.

We do not believe that major changes in CRA examinations are desirable. Some will argue that more banks should be eligible for streamlined exams; we believe that the recent changes went too far in making exams too easy for mid-size banks. Rigorous exams require more safe and sound lending from institutions.

CRA Enforcement Mechanisms

Mergers have traditionally been a major means of CRA enforcement but the frequency of mergers are likely to continue decline over the next several years. Consequently, additional enforcement mechanisms are needed. For instance, banks could be required to submit CRA improvement plans, subject to public comment, when they receive either a low rating overall or in any assessment area. CRA exams and merger approval orders could include an "expectations section" that either mandates or recommends (depending on the extent of the deficiency) improvements to specific aspects of CRA performance such as a particular type of lending or investment.

The agencies must also boost the rigor of the fair lending reviews that probe for evidence of illegal and discriminatory lending. Fair lending reports on CRA exams must be detailed explanations of the fair lending tests used instead of the one or two sentences currently on most CRA exams. In addition, the concept of illegal and discriminatory lending must be expanded to include unsafe and unsound lending. Banks have failed CRA exams because they made or financed unsafe loans; the fair lending review must routinely indicate whether the review found evidence of unsafe and unsound loans.

Some commentators will favor "incentives" to coax institutions into improved CRA performance. We would be supportive of exploring programmatic methods to increase tax credits under the Low Income Housing Tax Credits or New Markets Tax Credit for institutions receiving Outstanding ratings. But we are opposed to exemptions from CRA review on merger applications or decreasing the frequency of CRA exams for institutions with Outstanding ratings. CRA performance is likely to decline when institutions receive less frequent exams and public scrutiny.

Data Enhancements

By holding lenders accountable, publicly available data, particularly the Home Mortgage Disclosure Act, has been vital for increasing responsible lending to traditionally underserved borrowers. Applying a similar rationale, the limited CRA small business data must be enhanced to include the race and gender of the small business borrower. In addition, the agencies must require census tract level disclosure of community development loans and investments. In order to promote access to basic banking services, the agencies must require disclosure of enhanced data that shows types of deposit account (such as basic lifeline) by census tract location of the residence of bank customers. Likewise, data on the type consumer lending by borrower demographics and census tracts can promote access to affordable consumer loans and alternatives to abusive payday loans. Improvements in data disclosure will enhance the ability CRA exams to assess if banks are responsive to the full range of credit needs of communities.

Community Development

Some have suggested that banks receive favorable CRA consideration for investing in multi-regional funds for Low Income Housing Tax Credits and other purposes. In the interest of serving diverse geographical areas including rural areas, we are supportive of these suggestions as long as banks have adequately responded to the needs in their assessment areas. A bank could be required to have a rating of Outstanding on the investment test in most assessment areas, for example, before being allowed to invest outside of their assessment areas in multi-regional funds.

Conclusion

The severity of the foreclosure crisis would have been substantially lessened if the entire financial industry had an obligation to serve all communities consistent with safety and soundness. We believe that the regulatory agencies can contribute significantly to ensuring sustainable economic recovery by updating the CRA regulation. In addition, we believe that Congress must do its part and apply CRA to non-bank institutions including mainstream credit unions, independent mortgage companies, insurance firms, and investment banks.

Sincerely,

cc. The National Community Reinvestment Coalition

Endnotes

Sources for the research cited in this letter can be found in the testimony submitted by the National Community Reinvestment Coalition.

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