CATO INSTITUTE | Center for Monetary and Financial Alternatives

April 8, 2020

Federal Deposit Insurance Corporation
550 17th Street, NW
Washington, DC, 20429

Re: Community Reinvestment Act Regulations, A Proposed Rule by the Office of the Comptroller of the Currency and the Federal Deposit Insurance Corporation, Docket ID OCC-2018-0008, RIN 1557-AE34 and 3064-AF22

To Whom It May Concern,

I appreciate the opportunity to comment on the Notice of Proposed Rulemaking (Proposed Rule) describing changes to Community Reinvestment Act (CRA) regulations proposed by the Office of the Comptroller of the Currency and the Federal Deposit Insurance Corporation (the Agencies).

The Cato Institute is a public policy research organization dedicated to the principles of individual liberty, limited government, free markets, and peace. Cato's Center for Monetary and Financial Alternatives, at which I am a policy analyst, is dedicated to revealing the shortcomings of today's centralized, bureaucratic, and discretionary monetary and financial regulatory systems and to identifying, studying, and promoting alternatives more conducive to a stable, flourishing, and free society.

I thank Comptroller Otting and Chairman McWilliams for their leadership in the discussion of how CRA regulations can best promote financial inclusion and the well-being and prosperity of low- and moderate-income (LMI) communities.

Summary

The Proposed Rule would make a welcome update to CRA regulations, which have not been significantly revised since 1995. The Agencies' overarching goal—to provide much-needed clarity to banks about their future CRA evaluations—is laudable. However, three changes included in the Proposed Rule merit further consideration.

First, although the proposal's creation of deposit-based assessment areas, to complement existing facility-based ones, very properly acknowledges the growth of branchless banking and allows bank activities in "branch deserts" to be CRA-eligible, the threshold it applies in counting branchless deposits is excessively high. The Agencies should consider lowering it from 50 percent to 20 percent of retail domestic deposits, so that more banks can avail themselves of deposit-based assessment areas. To avoid having a lower threshold pose a heavy compliance burden for some institutions, the Agencies can make reporting of deposit-based areas voluntary for banks with branchless deposits between 20 and 50 percent of retail domestic deposits.

Second, although the Agencies' attempt to replace unclear qualitative evaluation measures with quantitative ratios responds to a longstanding complaint by banks, the proposed thresholds for converting these ratios into CRA ratings appear both arbitrary and capable of harming bank safety

and soundness. The Agencies should explain how they arrived at the thresholds proposed and offer proof that banks would be able to achieve adequate CRA ratings while still remaining safe and sound.

Third, by designating as "small" all banks with fewer than $500 million in assets, the proposed Rule would exempt many of the smallest banks and thrifts from burdensome CRA reporting and recordkeeping requirements. The Agencies should consider going further, however, by raising the "small bank" threshold to $1.5 billion. By also exempting banks presently designated as "intermediate small," this higher limit would still exempt a small share only (7.7 percent) of system assets.

The Agencies have also proposed to remove home mortgage loans to higher-income borrowers living in LMI areas from CRA-eligible activities. This change is long overdue. Between 2012 and 2017, around 65 percent of single-family mortgages eligible for CRA points in the District of Columbia went to higher-income borrowers. In the five largest Metropolitan Statistical Areas (MSAs), that share ranged from 18 percent to 56 percent. Higher-income borrowers were never the intended beneficiaries of the CRA, and including them in CRA evaluations does not directly benefit LMI households.

Introduction

The Community Reinvestment Act instructs federal banking regulators to encourage the institutions they supervise to "help meet the credit needs of the local communities in which they are chartered consistent with [their] safe and sound operation."[1] Since the CRA's passage in 1977, the three federal banking regulators—the Office of the Comptroller of the Currency (OCC), the Federal Deposit Insurance Corporation (FDIC), and the Board of Governors of the Federal Reserve System (Fed)--have periodically promulgated regulations to implement this mandate. The last major revision to CRA regulations occurred in 1995.[2]

The OCC is the most important CRA regulator, accounting for 66 percent of examined institutions by assets.[3] The FDIC and the Fed each examine around 16 percent of banks by the same measure, but the FDIC has a special role as the main regulator for the smallest U.S. banks, which struggle most to comply with the CRA, and especially to meet examiners' changing expectations.

The Proposed Rule was announced on December 12, 2019 by the OCC and FDIC only (the Agencies) and published in the Federal Register on January 9, 2020.[4] If the Fed does not align its regulations with the Agencies' final rule, the rule would apply to around 83 percent of U.S. banking system assets.

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[1] 12 U.S. Code § 2901.

[2] Federal Register, Vol. 60, No. 86 (May 4, 1995), p. 22156 ff. https://www.govinfo.gov/content/pkg/FR-1995-05-04/pdf/95-10503.pdf

[3] Treasury Memorandum to the OCC and FDIC on CRA Reform (April 2018), p. 28. https://home.treasury.gov/sites/default/files/2018-04/4-3-18%20CRA%20memo.pdf

[4] Federal Register, Vol. 85, No. 6 (January 9, 2020), p. 1204 ff. https://www.govinfo.gov/content/pkg/FR-2020-01-09/pdf/2019-27940.pdf

Why CRA Regulations Must Change

There are many reasons to update CRA regulations today. The U.S. banking sector has dramatically consolidated in the 25 years since the last significant changes were made to CRA regulations. Since 1995, the number of commercial banks has dropped by more than half, from 9,946 to 4,718, while the number of savings institutions has fallen by 66 percent, from 2,034 to 691. On the other hand, the number of commercial bank offices (headquarters plus branches) has grown, from 66,842 in 1995 to 82,731 in 2018, for a growth rate of 23.8 percent.[5]

Over the same period, improvements in communications technology have made it possible to provide a growing array of financial services remotely. Although national and state-chartered banks and thrifts continue to operate physical offices, their customers are increasingly able and willing to manage their financial affairs online.[6] Some established banks are also pursuing "branchless" growth strategies,[7] while several recently chartered ones are fully or mainly digital.[8]

These developments have rendered the 1995 CRA regulations unfit for their intended purpose. A major concern of policymakers at the time of the CRA's passage was banks' involvement in "capital export," meaning the collection of deposits in some communities to be lent in others.[9] The notion that deposits should remain in the communities where depositors live was never economically sound, as it ignores the principle of diversification and the fact that credit opportunities are not evenly distributed. Still, concerns about "capital export" were at least understandable in the 1970s, when state restrictions on branching limited bank competition.[10] In that context, banks with local monopolies or oligopolies were the main source of credit, and their refusal to lend locally could severely affect those localities' future growth prospects.

Banking industry consolidation and the growth of branches since 1995 have, however, increased competition in most U.S. local credit markets, undermining the market power of incumbents. Besides more local bank offices, households seeking credit today also have access to nonbank providers, which account for more than half of recent mortgage originations.[11] Today, LMI borrowers account for a bigger share of mortgage loans from nonbanks than banks, even though nonbanks are not subject to the CRA.[12]

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[5] FDIC, Historical Bank Data. Accessed March 10, 2020.

[6] According to a recent Accenture survey, a majority of consumers would like their banks to "blend physical and digital services," while more than 30 percent prefer to use mobile and tablet devices to communicate with their banks. See Accenture Global Financial Services Consumer Study, p. 39.

[7] Telis Demos, "No Branch, No Problem. Citigroup Bets Big on Digital Banking." *Wall Street Journal*, May 12, 2019.

[8] Ally Bank, a Utah state-chartered depository institution, has no branches. Recently, the OCC approved financial technology firm Varo Money's application for a national bank charter.

[9] Raymond H. Brescia, "Part of the Disease or Part of the Cure: The Financial Crisis and the Community Reinvestment Act," *South Carolina Law Review* Vol. 60 (2009), p. 630.

[10] Diego Zuluaga, "The Community Reinvestment Act in the Age of Fintech and Bank Competition," Cato Institute Policy Analysis No. 875 (July 10, 2019), p. 5-7. https://www.cato.org/sites/cato.org/files/pubs/pdf/pa-857-updated-2.pdf

[11] Consumer Financial Protection Bureau, "Data Point: 2017 Mortgage Market Activity and Trends," May 2018, p. 62. https://files.consumerfinance.gov/f/documents/bcfp_hmda_2017-mortgage-market-activity-trends_report.pdf

[12] Zuluaga, "The CRA in the Age of Fintech and Bank Competition," p. 14-15.

The OCC recognized both consolidation and technological change in a September 2018 Advance Notice of Proposed Rulemaking (ANPR) that anticipated the Agencies' Proposed Rule.[13] But there are other reasons as well for doubting the effectiveness of current CRA regulations. Evidence suggests that CRA lending has in some instances increased bank portfolio risk, even encouraging banks to make unsound loans.[14] More recently, I have shown that many, and sometimes most, home mortgages that could earn banks CRA points have actually gone to non-LMI borrowers. In the District of Columbia between 2012 and 2017, for example, around 65 percent of CRA-eligible single-family mortgages went to higher-income borrowers. For the five largest MSAs, the higher-income share of such mortgages was also high, up to 56 percent, and has steadily increased.[15]

The facts just outlined make this a propitious time to reform CRA regulations. Changes to the Proposed Rule should, however, seek not only to recognize the recent transformation of banking and increase certainty for banks, but to achieve the CRA's end of channeling credit, not just to local borrowers, but to local LMI households and in a safe and sound manner.

The OCC-FDIC Proposed Rule

The Proposed Rule has four goals: to clarify the activities that count for CRA points; to expand the range of qualifying activities; to introduce a more objective method for evaluating CRA performance; and to change data collection and reporting requirements in line with the other changes.[16] The Agencies seek to give banks certainty about which of their activities can earn them CRA points. Uncertainty regarding what counts, and how much, is a longstanding source of concern for banks, which previous studies of current CRA regulations have highlighted.[17]

The Proposed Rule's response to these concerns includes four separate changes to CRA regulations, each of which merits comment. They are: (1) the creation of deposit-based assessment areas; (2) the replacement of unclear performance criteria with quantitative measures; (3) the consolidation of "small" and "intermediate small" bank designations into one new "small bank" category; and (4) the removal of home mortgage loans to high-income borrowers living in LMI areas from the category of retail lending activities eligible for CRA points.

Creating Deposit-Based Assessment Areas

When the CRA was enacted, representatives in Congress worried that some communities lacked sufficient bank capital to grow and thrive. Restrictions on bank branching and deposit interest

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[13] Federal Register, Vol. 83, No. 172 (September 5, 2018), p. 45054. https://www.govinfo.gov/content/pkg/FR-2018-09-05/pdf/2018-19169.pdf

[14] Jeffery W. Gunther, "Safety and Soundness and the CRA: Is There a Conflict?" *Economic Inquiry* Vol. 40, No. 3 (July 2002): 470-484, https://onlinelibrary.wiley.com/doi/full/10.1093/ei/40.3.470; Sumit Agarwal, Efraim Benmelech, Nittai Bergman, and Amit Seru, "Did the Community Reinvestment Act (CRA) Lead to Risky Lending?," Kreisman Working Papers Series in Housing Law and Policy no. 8, October 2012, https://papers.ssrn.com/sol3/papers.cfm?abstract_id=2172549; Mark Willis, "It's the Rating, Stupid: A Banker's Perspective on the CRA," in *Revisiting the CRA: Perspectives on the Future of the Community Reinvestment Act*, eds. Prabal Chakrabarti, David Erickson, Ren S. Essene, Ian Galloway, and John Olson, Federal Reserve Banks of Boston and San Francisco (February 2009), p. 61, https://www.frbsf.org/community-development/files/revisiting_cra.pdf.

[15] Diego Zuluaga, "More Evidence that the CRA Doesn't Always Help Low-Income Communities. But Proposed Changes Will Improve It." *Alt-M*, January 28, 2020, https://www.alt-m.org/2020/01/28/more-evidence-that-the-cra-doesnt-always-help-low-income-communities-but-proposed-changes-will-improve-it/.

[16] See Proposed Rule, p. 1208-1209.

[17] Treasury Memorandum (April 2018), p. 11 and Joint Agencies' Report (2017), p. 45.

rates prevalent at the time may have justified this concern.[18] Today, however, the vibrant competition among banks and nonbanks is prompting both to lend more widely across U.S. communities. This is helping to redress the legacy of redlining and making concerns about "capital export" less urgent than they were in 1977. Still, current CRA regulations may make it more difficult for banks to serve sparsely populated areas where they do not operate branches, while failing to take account of the growing trend for some banks to take deposits and offer financial services without local branches.[19]

The Proposed Rule would address these important shortcomings by giving CRA points to banks that serve areas without local bank offices[20] and, more significantly, by allowing banks with a large share of deposits from areas where they do not operate offices or ATMs to count lending in those areas toward their CRA evaluations.[21] Specifically, under the Proposed Rule, banks that collect more than 50 percent of their retail domestic deposits outside their facility-based assessment areas—-that is, the areas where they have offices or ATMs—-would report their lending in all "branchless" areas where they collect more than 5 percent of deposits.[22]

Counting loans to "branch deserts" can benefit many rural communities across America. Likewise, counting loans and other bank activities in areas where a bank has no branches or ATMs, but where many of its depositors reside, will better fulfill the spirit of the CRA, namely, to ensure banks serve the credit needs of the communities where they take deposits. Current regulations, because they only examine areas where banks have physical facilities, ignore a growing proportion of bank deposit-taking and lending activity. The Proposed Rule does well to fix this.

It is surprising, however, that the Agencies would set what seems a high threshold to begin counting loans in branchless areas. Some banks operate fully without physical facilities and would be able to define deposit-based assessment areas under the 50-percent criterion of the Proposed Rule. But many more banks capture a small but growing share of their deposits online, even if it remains far from the 50-percent threshold. Refusing to count related lending activity as part of those banks' CRA performance would be a missed opportunity for the communities where their online depositors live.

The Agencies should therefore consider lowering the threshold for deposit-based definition of assessment areas to 20 percent of a bank's domestic retail deposits. If the Agencies are concerned that such a low threshold might place a new compliance burden on banks, they could make deposit-based assessment area definition voluntary for banks with a branchless deposit share between 20 and 50 percent. Similarly, the Agencies might retain mandatory definition of deposit-based assessment areas wherever banks collect more than 5 percent of deposits, but give banks discretion to define additional assessment areas where they collect a substantial proportion of deposits below that amount.

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[18] Zuluaga, "The CRA in the Age of Fintech and Bank Competition," p. 7.
[19] See Joint Agency Report, p. 42: "Numerous community group and industry commenters observed that the assessment area definition no longer reflects the way in which financial services are delivered." https://www.ffiec.gov/pdf/2017_FFIEC_EGRPRA_Joint-Report_to_Congress.pdf
[20] Proposed Rule, p. 1212.
[21] Proposed Rule, pp. 1215-1216.
[22] Ibid., p. 1216.

A Quantitative Approach to Performance Evaluations

The Agencies have proposed several quantitative measures that they believe will, in combination, accurately reflect banks' community reinvestment performance. The proposed measures take the form of demographic, peer-comparator, and deposit ratios.[23] Demographic ratios measure bank lending to LMI borrowers and small businesses as a percentage of their total lending in the assessment area. Peer-comparator ratios compare a bank's lending to LMI borrowers and small businesses with its peers in the assessment area. Finally, deposit ratios relate banks' assessment-area lending and community development activities to their average quarterly deposits.

The agencies make a persuasive case that the current evaluation approach is opaque and uncertain, leaving important terms such as "excellent" and "good," which supposedly describe a bank's performance, undefined.[24] In its April 2018 memorandum on CRA reform, the Treasury expanded on this critique, calling "for an approach to the administration of [the] CRA that incorporates less subjective evaluation techniques."[25] Banks also support more transparent evaluation criteria that will allow them to estimate their likely performance before an examination.[26]

While the Agencies' goal of a more objective evaluation approach is laudable and the problems with the existing approach are well-known, the ratios in the Proposed Rule present challenges of their own. The most obvious is that ratios would require banks to collect industry-level data on lending, deposits, and other bank activities to which they may lack ready access. Some information may be available from government databases compiled under other statutory authorities, such as the HMDA and Call Report databases maintained by the Consumer Financial Protection Bureau and the prudential banking regulators, respectively. Still, that data becomes public with a time lag and is not complete, potentially requiring banks to make extrapolations and assumptions without regulatory sanction.[27]

An additional challenge is the choice of performance thresholds above which a bank would earn a given CRA rating. The Proposed Rule notes that banks would need to earn a "satisfactory" or "outstanding" rating in at least 50 percent of its assessment areas in order to be awarded such a rating for its overall performance.[28] But the Agencies do not explain their choice of performance thresholds (55 percent or higher for the demographic ratio, and 65 percent or higher for the peer-comparator ratio) in the small-business loan example they cite.[29] Even if the Agencies are reluctant to publish the full set of calculations that led to these thresholds, they should consider specifying whether they chose thresholds that would earn banks similar ratings to what they have

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[23] Proposed Rule, pp. 1218-1221.
[24] Ibid., p. 1217.
[25] Treasury memorandum, p. 11.
[26] Krista Shonk, "Re: Reforming the Community Reinvestment Act Regulatory Framework," Docket ID OCC–2018–0008, American Bankers Association, November 15, 2018, p. 7. https://www.aba.com/-/media/documents/comment-letter/cl-cra20181115.pdf?rev=a8d598e9460341e78a4d76aa004dd244
[27] The Agencies themselves had to resort to assumptions when estimating individual banks' performance under the Proposed Rule. See pp. 1221-1222.
[28] Proposed Rule, p. 1217.
[29] Ibid., p. 12

earned in the past, or ones that assess bank performance more strictly than in the past, or if they had a different goal in mind.

Any quantitative performance measure will involve some arbitrary discretion on the part of regulators. Indeed, it is questionable that regulators can ever know how much lending a community needs, and whether an individual bank's lending activity falls above or below its rightful share. But even if today's thresholds are optimal, banks have no assurance that they will remain unchanged. On the contrary, it might prove all too tempting to raise the thresholds in the future in a bid to increase bank lending in LMI communities. Even if such additional lending threatens banks' safety and soundness, the deleterious effects will only become apparent in subsequent examinations.

The Agencies should therefore guard against future ill-advised changes to the quantitative measures they set in the final rule. Addressing such an eventuality is essential if the Agencies are to fulfil the CRA's mission of promoting lending across communities, consistent with safety and soundness. To that aim, the Agencies should carefully explain why they chose the thresholds in the Proposed Rule, and how their approach balances the promotion of credit with prudential goals. Doing so increases the chances that future regulators, should they seek to raise the thresholds, will be compelled to offer a similar justification.

Changes to the "Small Bank" Qualifying Criteria and Evaluation

The Agencies propose to change the definition of a "small bank" for purposes of CRA evaluations. This designation provides for a narrower set of performance standards focused mainly on assessment-area retail lending.[30] It also exempts banks that meet the designation from the CRA's record-keeping requirements.[31] In addition, the Agencies would eliminate the "intermediate small bank" designation for banks with assets above the "small bank" threshold but below another, higher limit (currently, $1.284 billion). Examinations of intermediate small banks are currently also less comprehensive than those for larger banks.[32]

The Proposed Rule would lift the small bank asset threshold from $321 million (as of end-2019) to $500 million. Small banks under the Proposed Rule could opt into the general performance evaluation in the Proposed Rule, but they could also choose to be evaluated under the small bank performance standards of current CRA regulations. Lifting the threshold to $500 million means nearly three-quarters of banks would be small banks and therefore have a choice of CRA evaluation criteria. Such flexibility recognizes the compliance challenges small banks face simply in adapting to changing regulatory practices.

Because the U.S. banking system has 5,186 banks and thrifts at last count, with around 100 large institutions and thousands of very small ones, an asset threshold such as the one proposed can exempt many institutions from onerous compliance costs, while affecting only a small proportion of total banking system assets.[33] The threshold the Agencies suggest in the Proposed Rule, for

[30] 12 C.F.R. § 25.26.
[31] Proposed Rule, p. 1227.
[32] 12 C.F.R. § 25.26.
[33] The calculations in this section are the author's own using FDIC Call Report data for the quarter ending Dec. 31, 2019.

example, would treat 72 percent of banks and thrifts as small banks for CRA purposes, but these institutions account for just 3.7 percent of total bank and thrift assets.

Lifting the small bank threshold higher might be advisable in order to minimize the additional compliance burden on relatively small institutions, without exempting a large share of banking assets from the general CRA performance standards. An asset threshold of $1 billion, for example, would give flexibility to the smallest 84.5 percent of banks and thrifts, which jointly account for just 6.2 percent of assets, while a $1.5 billion threshold would benefit 89 percent of banks and thrifts representing 7.7 percent of assets. Clearly, a generous small bank threshold comes at relatively low supervisory cost, so the Agencies should consider lifting it to $1.5 billion. This threshold would cover all banks that currently are either small or intermediate small.

Removing High-Income Households from CRA Consideration

The CRA aims at ensuring safe and sound credit provision to all income groups within a community. Regulators have long interpreted this mandate as one to evaluate banks for their lending, investment, and services provision to LMI borrowers and communities.[34] A LMI borrower has median family income below 80 percent of its MSA's median family income, while a LMI community is a census tract where the median family income is 80 percent or less of the surrounding MSA.[35] But current CRA regulations instruct examiners to consider mortgage loans to high-income borrowers, so long as they live in LMI communities.[36] The Proposed Rule would no longer count such loans in banks' CRA evaluations. As the Agencies note:

> *Unlike small loans to businesses and small loans to farms in LMI areas that may result in additional job creation or other positive effects for the larger community, home mortgage and consumer loans to middle- or upper-income individuals and families in LMI areas are generally not as beneficial to LMI communities and may result in displacement.*[37]

This change is both important and necessary. Banks have long complained that it is not possible to establish with certainty which individual loans currently serve to improve their CRA scores.[38] The Agencies seek to provide clarity by publishing a long list of qualifying activities as part of their proposal.[39] But current rules define which loans within a bank's assessment area are *eligible* for CRA points. Specifically, mortgage loans to LMI borrowers anywhere in a bank's assessment area are eligible for CRA points, as are any mortgage loans in LMI census tracts within an assessment area (Figure 1).

[34] 12 C.F.R. § 25.21.
[35] Ben Horowitz, "Defining 'Low- and Moderate-Income and 'Assessment Area,'" Federal Reserve Bank of Minneapolis, March 8, 2018, https://www.minneapolisfed.org/article/2018/defining-low--and-moderate-income-and-assessment-areas.
[36] 12 C.F.R. § 25.11.
[37] Proposed Rule, p. 1219.
[38] *ABA Banking Journal*, "Bonus Podcast: Key Points on CRA Modernization," American Bankers Association, November 14, 2018, podcast audio, 4:10, https://bankingjournal.aba.com/2018/11/bonus-podcast-key-points-on-cra-modernization/.
[39] Proposed Rule, pp. 1229-1234.

Figure 1: Loans to Low-Income Borrowers and in Low-Income Census Tracts Qualify for CRA Points

Census tract LMI, Borrower LMI	**Census tract non-LMI, Borrower LMI**
Census tract LMI, Borrower non-LMI	**Census tract non-LMI, Borrower non-LMI**

Source: Diego Zuluaga, "More Evidence that the CRA Doesn't Always Help Low-Income Communities. But Proposed Changes Will Improve It." Alt-M, January 28, 2020, https://www.alt-m.org/2020/01/28/more-evidence-that-the-cra-doesnt-always-help-low-income- communities-but-proposed-changes-will-improve-it/.

There are several reasons why counting non-LMI loans in evaluations is inappropriate. Non-LMI households have not historically faced the same difficulties in gaining access to credit as LMI ones. That is because higher-income loan applicants are more likely to be approved. There is also a strong correlation between race and income: Minorities, long the targets of institutional redlining, have considerably lower median family incomes and a higher proportion of underbanked households than white non-Hispanic Americans.[40]

Counting non-LMI loans in LMI areas may also have counterproductive effects. In recent years, there has been a trend of rapid neighborhood change in many U.S. cities. Often that trend has involved gentrification, the process by which middle-and upper-income arrivals replace the historic lower-income residents of a neighborhood.[41] While gentrification remains a controversial subject, a recent study from the Federal Reserve Bank of Philadelphia finds that it tends to improve the welfare of the original residents, including those who do not own their homes and lack a college education. On the other hand, the study finds only a small increase in out-migration as a result of gentrification.[42]

The average impact of gentrification on displacement may therefore be lower than some have previously argued. Still, there are concerns that gentrification may drive displacement in specific contexts, for example, when housing supply is unresponsive to rising demand due to zoning restrictions. Anecdotal reports suggest that "gentrifiers" have become significant recipients of CRA-related lending, raising concerns that the law as implemented no longer promotes its original mission.[43] A large share of higher-income borrowers among CRA-eligible loans would also explain

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[40] Gloria G. Guzman, "Household Income: 2018," American Community Survey Brief, September 2019, p. 8, https://www.census.gov/content/dam/Census/library/publications/2019/acs/acsbr18-01.pdf; Federal Deposit Insurance Corporation, "2017 FDIC National Survey of Unbanked and Underbanked Households," October 2018, p. 19, https://www.fdic.gov/householdsurvey/2017/2017report.pdf.

[41] Ruth Glass was the first to use the term "gentrification" to refer to neighborhood change in London. See Ruth Glass, *London: aspects of change* (MacGibbon & Kee, 1964).

[42] Quentin Brummet and Davin Reed, "The Effects of Gentrification on the Well-Being and Opportunity of Original Resident Adults and Children," Working Paper 19-30, July 2019, pp. 17-20. https://www.philadelphiafed.org/-/media/research-and-data/publications/working-papers/2019/wp19-30.pdf

[43] Aaron Glantz and Emmanuel Martinez, "Gentrification Became Low-Income Lending Law's Unintended Consequence," *Reveal*, February 16, 2018, https://www.revealnews.org/article/gentrification-became-low-income-lending-laws-unintended-consequence/.

the finding that borrowers within assessment areas have higher credit scores than those outside them.[44]

In fact, higher-income borrowers make up a very large share of CRA-eligible mortgage lending. Using data from recent Home Mortgage Disclosure Act (HMDA) filings, I have found that, in the District of Columbia between 2012 and 2017, single-family mortgages to non-LMI borrowers living in LMI areas accounted for around 65 percent of all CRA-eligible mortgages.[45] For the top five MSAs in the United States, the share of high-income mortgages among CRA-eligible mortgages ranged between one-fifth and more than half of loan volume. Furthermore, that share increased across all five MSAs between 2012 and 2017 (Table 1).[46]

Table 1. Share of CRA-Eligible Single-Family Mortgages to High-Income Borrowers, by MSA and Year (%)

MSA	2012	2013	2014	2015	2016	2017
Chicago-Naperville-Arlington Heights, IL	18.04	21.71	23.95	23.98	30.37	31.41
Dallas-Plano-Irving, TX	17.53	18.97	26.18	28.12	33.06	36.18
Houston-The Woodlands-Sugar Land, TX	21.96	24.86	34.10	32.24	37.37	39.55
Los Angeles-Long Beach-Glendale, CA	27.33	29.55	45.32	40.80	41.38	48.69
New York-Jersey City-White Plains, NY-NJ	44.79	47.65	53.13	52.61	53.73	55.66

Source: Home Mortgage Disclosure Act database.

The late 1970s, when the CRA became law, was a time of urban flight and decline. Encouraging higher-income residents to remain in cities rather than move to suburbs may have had some justification then, although the impact of the CRA can only have been minor. Regardless, the late 2010s and early 2020s are a time of rapid urban renewal and gentrification. Better-off homebuyers need no regulatory assistance.

Conclusion

The Proposed Rule is a step in the right direction. It would introduce greater certainty into CRA evaluations, simplify the small bank designation, acknowledge the growing importance of branchless deposits, and focus evaluations on LMI borrowers. While there are potential problems with the performance ratios in the Proposed Rule, a more detailed explanation of how the Agencies chose the ratings thresholds can help mitigate future abuse of those ratios, thereby helping to assure bank safety and soundness.

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[44] Neil Bhutta and Glenn B. Canner, "Mortgage Market Conditions and Borrower Outcomes: Evidence from the 2012 HMDA Data and Matched HMDA–Credit Record Data," Federal Reserve Bulletin Vol. 99, No. 4 (November 2013), p. 34, https://www.federalreserve.gov/pubs/bulletin/2013/pdf/2012_HMDA.pdf.

[45] Diego Zuluaga and Andrew Forrester, "The Impact of the Community Reinvestment Act on Neighborhood Gentrification," *Quarterly Journal of Finance and Accounting* (forthcoming).

[46] Diego Zuluaga, "More Evidence that the CRA Doesn't Always Help Low-Income Communities. But Proposed Changes Will Improve It." *Alt-M*, January 28, 2020, https://www.alt-m.org/2020/01/28/more-evidence-that-the-cra-doesnt-always-help-low-income-communities-but-proposed-changes-will-improve-it/.

I hope the Agencies will find this submission helpful, and that they will consider its recommendations as they prepare a final rule. Please do not hesitate to contact me at DZuluaga@cato.org if you have any questions.

Yours sincerely,

[redacted]

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