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October 17, 2001

Communications Division
Mailstop 1–5
Office of the Comptroller of the Currency
250 E Street, SW
Washington, DC 20219
Re: Docket No. 01–16

Robert E. Feldman, Executive Secretary
Attention: Comments/OES
Federal Deposit Insurance Corporation
550 17th Street, NW
Washington, DC 20429
Re: 12 CFR Part 345; RIN 3064–AC50

Ms. Jennifer J. Johnson, Secretary,
Board of Governors of the
Federal Reserve System
20th Street & Constitution Avenue, NW
Washington, DC 20551
Re: Docket No. R–1112

Regulation Comments
Chief Counsel's Office
Office of Thrift Supervision
1700 G Street, NW
Washington, DC 20552
Re: Docket No. 2001–49

Re: Advance Notice of Proposed Rulemaking on the Community Reinvestment Act Regulations; 66 Federal Register 37602; July 19, 2001

Dear Madams and Sirs:

On July 19, 2001, the Federal Deposit Insurance Corporation ("FDIC"), the Federal Reserve Board, the Office of the Comptroller of the Currency, and the Office of Thrift Supervision (the "Agencies" or "regulators") published a Joint Agency Advance Notice of Proposed Rulemaking ("ANPR") as part of their review of the Community Reinvestment Act ("CRA") regulations. As the Agencies expressed it, the ANPR begins "our assessment of the effectiveness of the regulations in achieving their original goals of (1) emphasizing in examinations an institution's actual performance in, rather than its process for, addressing CRA responsibilities; (2) promoting consistency in evaluations; and (3) eliminating unnecessary burden." The Community Reinvestment Act applies to all FDIC-insured depository institutions, most of which are members of the American Bankers Association ("ABA"). The American Bankers Association brings together all categories of banking institutions to best represent the interests of this rapidly changing industry. Its membership – which includes community, regional and money center banks and bank and financial holding companies, as well as savings associations, trust companies and savings banks – makes ABA the largest bank trade association in the country.

Introduction

The ANPR consists of a number of broad questions about the application of the CRA regulations to depository institutions. However, initially the Agencies raise a threshold question, which a number of bankers have also raised in the last year: whether any change to the regulations would be beneficial or warranted. ABA believes that any change to the CRA regulations needs to be evaluated not only for the benefit it would bring but also for the cost imposed to make the change. In other words, is the cost worth the benefit? Additionally, many bankers have expressed concern that a request for major changes will result in worse regulations. While the 1995 revision did improve CRA examinations and procedures for those banks under $250 million, banks subject to the large bank examination feel that many new requirements were added by the Agencies that made CRA even more burdensome. For example, a data collection and reporting requirement was added and new investment and service tests were created. While the new examination was meant to reduce paperwork and regulatory burden, in practice the large bank examination has led to greater complication of the regulations and more paperwork burden. Many large banks report that they must keep extensive records and carefully document their loans and investments in order to be sure that examiners will give CRA credit for them. The last thing these bankers want is a revision that makes the large bank examination even more difficult and burdensome. Thus ABA is reluctant to request major changes except where necessary. Changes should increase the flexibility of banks to comply with the requirements of the Act without significantly increasing burden. Nonetheless, ABA believes some changes are needed to the CRA regulations. ABA's recommendations are set out below, following the order of issues listed by the Agencies in the ANPR.

Recommendations

1. Large bank exam: investment, lending and service tests

The Agencies ask if the regulations strike the appropriate balance between quantitative and qualitative measures, and among lending, investments, and services. ABA believes that, currently, the regulations do not have an appropriate balance. The primary focus of the Community Reinvestment Act is the requirement that the Agencies evaluate insured depository institutions for how well the institutions are helping to meet the credit needs of the entire community. ABA believes that the regulations shift their focus too much away from the issue of credit and place too much emphasis on community development and investments. **ABA recommends that the investment test be eliminated. Rather, investments should be substitutable for loans.** This recommendation is detailed further in the discussion of the individual tests that follows.

The Agencies ask whether CRA evaluations have become simply a "numbers game" or the regulations strike the right balance between evaluation of the *quantity* and *quality* of CRA activities. Some of our bankers do believe that their CRA examinations are increasingly becoming a numbers game. In particular, loans with longer terms appear to be discounted or not considered by examiners after the first few years of their term. (Some bankers relate that their examiners continue to count these loans, adjusting for the declining balances on them.) Bankers also report that examiners seem to expect ever-increasing levels of certain loans, such as community development loans or LMI loans, leading bankers to conclude that there is an ever-increasing demand for higher levels of lending in certain categories. Many bankers are expressing concern that the levels of lending now expected of them would have been simply unsustainable, even if the economy had continued to grow at its 1990s pace. Certainly these levels of lending are not sustainable now, and bankers are concerned that examiners do not understand the performance context of these institutions or these types of lending. **ABA urges the Agencies to seriously review this "sustainability" issue in examiner guidance, as it is of great concern to a number of bankers that ABA consulted on this CRA ANPR.**

The Agencies also ask whether the regulations provide too little consideration for an institution's focus on smaller projects, whether or not "innovative", that are particularly difficult to carry out, but are especially meaningful and responsive to the institution's community. Many of our bankers have expressed frustration that examiners seem to be requiring new evidence of more "innovation and complexity" at each examination. **ABA recommends that examination guidance should more clearly state that while innovation and complexity may add to the value of a CRA loan, service or investment, a financial institution is not required to demonstrate that some percentage of its lending and investments are innovative or complex or else the institution will be downgraded for failing to be innovative and complex.** Financial institutions that are doing significant conventional lending into their communities should be rated Satisfactory, not criticized for not being innovative and complex.

Lending Test Issues

The Agencies ask if the regulations should continue to treat originations equal with purchases or should originations count for more than purchases. Community groups and some regulators feel that banks that make the extra effort to keep open branches in LMI areas, make special outreach efforts and otherwise do the extra steps to originate LMI loans are not getting recognition for these efforts, and so suggest that originations should count for more than purchases. However, the Act itself makes no such distinction. As both originations and purchases increase the flow of credit and as purchases of loans from originating banks free up their funds to make additional loans, ABA sees little value in discouraging loan purchases. **ABA recommends not making any change. Attempts to value originations and purchased loans differently will introduce an unnecessary level of complexity for little benefit under the statute.**

On the issue of whether CRA ratings should include a negative impact for predatory lending, ABA is concerned that such an addition will be difficult to formulate and implement and will provide little additional benefit. ABA believes that the most difficult issues to resolve in such a change would be just how to define predatory lending and how to establish what due diligence would be required of banks lending to third party lenders or investing in mortgage-backed securities. There is little agreement on these issues, as demonstrated by the wide variation in what proposed and enacted state legislation and local ordinances define as predatory lending. The Agencies know how difficult it is to attempt to define objectively what is a predatory loan. Further, under the current regulations, fair lending violations may lower a bank's CRA rating. Since predatory lending is generally thought to target illegally potential victims on the basis of gender, race, age or other protected basis under the fair lending laws, **ABA recommends that predatory lending continue to be part of the fair lending examination, and not made an additional component of the CRA regulations.**

Investment Test Issues

The Agencies ask if the investment test effectively assesses an institution's record of helping to meet the credit needs of its entire community. ABA believes that the investment test does not. The number one problem with CRA that bankers (rated under the large bank exam) mention is the investment test[1] or issues related to it. However, very large banks with large community development programs tend to want more credit and wider scope for their investments (including credit for investments outside of their assessment areas), while the vast majority of the remaining banks want less or no investment test and less rigid requirements for investments to qualify for CRA credit.

ABA recommends that the investment test be eliminated. Rather, investments should be substitutable for loans. There would be no separate level of investments required of banks, but certain investments would be countable towards the lending test. While this may appear to be a major change, it solves many of the specific problems that are mentioned as issues in the ANPR and greatly increases banks' flexibility in complying with CRA. Large banks committed to major community development lending programs in urban MSAs will continue to receive CRA credit for their important activities while smaller banks will not be forced to search for investment opportunities that do not exist for them in their markets.

ABA has long objected to the investment test on several grounds. First, ABA believes that the Community Reinvestment Act simply does not authorize the Agencies to impose a separate "investment test" for CRA, and therefore the Agencies should eliminate it. See Appendix 1.

However, more importantly, the establishment of a separate "investment test" by the Agencies has created a number of practical problems under the regulations that need resolution. First, bankers tell ABA that the definition of qualified investments is too narrow. This narrowness of the definition results in many valuable community activities and investments that benefit the entire community but not the specific LMI areas targeted by the regulations being excluded from consideration under CRA. This results in banks having to pass up real opportunities to support their communities in favor of investments acceptable to the Agencies. The most prominent example of this effect is seen in the treatment of the investment by smaller banks in municipal obligations of their communities. Now under current CRA interpretations, these municipal bonds must be targeted to low- or middle-income residents or narrow community development programs or else banks cannot receive credit for their investments. Thus investments, including grants and charitable contributions, by banks are funneled by the Agencies into very specific types of activities and recipients. Again, while these goals may be laudable, the authority for the Agencies to establish these goals and also to exclude other community investments from CRA consideration is not provided in the Community Reinvestment Act.

It is instructive to list some of the things that the Agencies will not count for CRA. For example, grants to United Way appear not to qualify for CRA investment credit, as many United Way

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[1] The investment test is established by §__.23. The investment test "evaluates a bank's record of helping to meet the credit needs of its assessment area(s) through qualified investments that benefit its assessment area(s) or a broader statewide or regional area that includes the bank's assessment area(s)." [Emphasis added.] A "qualified investment" is defined in §__.12(s) as "a lawful investment, deposit, membership share, or grant that has as its primary purpose community development." Community development is defined in §__.12(h) as follows:

Community development means:

(1) Affordable housing (including multifamily rental housing) for low- or moderate-income individuals;

(2) Community services targeted to low- or moderate-income individuals;

(3) Activities that promote economic development by financing businesses or farms that meet the size eligibility standards of the Small Business Administration's Development Company or Small Business Investment Company programs (13 CFR 121.301) or have gross annual revenues of $1 million or less; or

(4) Activities that revitalize or stabilize low- or moderate-income geographies.

organizations do not target just low- and moderate-income people. Only if the bank specifies that its contribution is targeted to a particular recipient, like a homeless shelter, will CRA credit be given by examiners. Contributions to the American Lung Association, the American Diabetes Association and other organizations devoted primarily to health research for the entire community, or even their community-based local chapters, do not appear to qualify for CRA credit. Other organizations that do not clearly target low- and moderate-income persons or neighborhoods or revitalize or stabilize LMI geographies include most museums, most orchestras and performing arts organizations, and many other civic or community-based organizations. Yet most people would consider support of such organizations as "community reinvestment." Investments and loans that help bring a major new company to a community, if the company exceeds the small business revenue limits, may not be "community development" unless the bank can convince examiners that the company's presence will "revitalize or stabilize low- or moderate-income geographies."

The Community Reinvestment Act mandates that the bank regulators encourage banks to serve their entire communities, including any low- and moderate-income ("LMI") neighborhoods. ABA believes that the current regulations instead actively direct investments and lending into LMI neighborhoods or into specific kinds of LMI community development lending or investments by giving little or no CRA credit for lending or investments that benefit the entire community, including LMI neighborhoods. ABA believes that this steering of credit and investment by the Agencies was not intended by the Congress and is not authorized by the Community Reinvestment Act.

Second, the investment test and the narrow definitions of what qualifies for CRA credit result in banks paying a premium for qualified investments, since there is more demand than supply. ABA believes such premiums result in an economic loss to the community. The CRA regulations define "qualified investments" as those having a primary purpose of community development. By narrowly defining what qualifies, the regulations have decreased the pool of "qualified investments" available to banks and savings associations. Repeatedly, ABA has been told by smaller banks subject to the large bank investment test that they are unable to compete with multi-billion dollar banks for a share of the limited pool of qualifying investments. This is particularly true now because many large banks are competing heavily for the limited pool of qualified investments as insurance that they will pass the investment test. Even small banks that are examined under the small bank examination have experienced this drought in opportunities to make qualified investments, which they need in order to boost their ratings from a Satisfactory to an Outstanding, a goal of many small banks that are proud of the role they play in their communities.

Banks now observe that many "CRA qualified investments" now have more "regulatory value" than they have "market value," creating a "CRA premium" for that small pool of investments that meet the Agencies' requirements for CRA. More dollars chase fewer good investments because of the regulatorily-induced need for at least a low satisfactory component in the investment test. These concerns do not question the value of "qualified investments" to a community or to a bank, but they does raise difficult questions about the market value versus the social or regulatory value of some of these investments.

As one banker of an approximately $2 billion bank expressed it to ABA recently, "What I have been finding during the last two years since our CRA exam is that the CRA investments that I am finding are not profitable. In many cases, the rates of return are at or below our cost of funds, and the minimum purchase is $1-2 million. This may not sound like it is 'too large' of an investment, but most investments we make are in the $100,000 - $200,000 range. Occasionally we have invested up to $1 million when the tax-equivalent yields are in the same range as our commercial loan rates. In addition to being large amounts at a low rate, the term is generally 30 years. Since we are at (or near?) the bottom of the interest rate market right now, the interest rate risk of such an investment is substantial. I don't believe it was the intent of CRA to force community banks to make investments that could threaten their survival but that is what is happening."

Third, the regulations in general and the investment test in particular have resulted in greater documentation burden. In order to demonstrate to examiners that their loans and investments qualify for CRA credit, banks must thoroughly document that the regulations' definitions are met. Further, the regulations on investment are so vague and restrictive that they confuse both bankers and examiners. In fact, the primary purpose of the numerous revisions to the CRA Questions and Answers has been to try to clarify the application of the "community development" requirements and the workings of the investment test.

The result of all of this regulatory clarification of the Community Reinvestment Act is a constant debate between banks and examiners over whether particular loans and investments qualify for CRA credit under these narrow definitions. The result is an increase in paperwork as institutions seek to demonstrate that a particular loan or investment is sufficiently targeted towards low- and moderate-income residents or geographies or sufficiently revitalizes or stabilizes LMI geographies to receive CRA credit. The result is a channeling of credit to specific geographies of a community or certain community organizations rather than an evaluation of the bank's record of helping to meet the credit needs of the <u>entire</u> community. And the result is not authorized by the Community Reinvestment Act.

Finally, bankers report that actual examination practice in determining whether a particular investment qualifies for CRA consideration is inconsistent among the Agencies and even among regional offices and districts of the same Agency. This is most evident to banks in the same holding company but under different regulators, but has been reported by banking organizations with banks under the same regulator but in different districts. While part of this may reflect a need for better training, we believe much of it stems from the regulations themselves, particularly with respect to qualified investments.

For all of these reasons, ABA concludes that the investment test should be eliminated. If the investment test is eliminated and investments are made substitutable for loans under the lending test, the problems just discussed are resolved or reduced. First, many smaller banks have no problems with the lending test but have problems in meeting the investment test as a separate and additional requirement, because of the scarcity of qualifying investments in their communities. This problem is eliminated. Many large banks are committed to community development investment and will continue to make these investments, but with this change these banks would have more flexibility in structuring loans and investments, since both will be includable under the lending test. By reducing the regulatory demand for investments, the CRA "premium" on qualifying investments should decline or disappear. And disagreements between banks and examiners over "qualifying investments" should be diminished, since banks will not be required to make a certain level of investment. This should reduce the unnecessary regulatory burden that has been imposed as part of the investment test.

If investments are made substitutable for loans, there is the further question of whether they should substitute "dollar for dollar" or should some other formula be used in converting investments into an equivalent of a loan. **ABA recommends that CRA credit for investments needs to be**

adjusted for the cost of the capital to support the investments, when substituting investments for loans. For example, a grant that qualifies as a "CRA qualified investment" would be roughly equivalent to a loan ten times the amount of the grant, since the capital required of a well-capitalized bank is 10% of the loan, but a grant consists of 100% capital that will not be recovered. The proposed capital cost valuation for true investments as well as for grants should be incorporated into the CRA regulations' overall definition of "qualified investment." Doing so will benefit all banks irrespective of their evaluation method - small bank, limited purpose, strategic plan, or large bank. Further issues in finding an equivalency between investments and loans arise with consideration of the duration of the loan or investment. These questions will need to be addressed in subsequent rulemaking.

The Agencies ask if investments should be considered at all under CRA. If so, should they only be considered as to whether an institution with a Satisfactory rating deserves to have an outstanding rating? As discussed above, ABA believes that investments should be substitutable for loans, but should not be a separate requirement or test. The Agencies appear to be suggesting that investments (and services, see below) be treated as possible extra credit, but only if the bank's lending was Satisfactory by itself. While this would return the focus of the CRA regulations to lending and to helping to meet the credit needs of the community, it does not provide for full substitution of an investment for a loan. **There are some investments that are so close to loans in their effect that they should always count towards helping to meet the credit needs of the community. Other investments, such as grants for charities or community organizations, are not that clearly the equivalent of loans. The Agencies could treat those investments only as extra credit, if the bank already had a Satisfactory rating. ABA would be interested in seeing additional development of this concept by the Agencies. If the Agencies are suggesting that lending by itself, no matter how outstanding, could only earn a bank a Satisfactory rating and then the bank would have to show additional investment or service to earn an Outstanding rating, ABA opposes that suggestion as contrary to the statute.**

Even if the investment test is eliminated, ABA still thinks that the definition of qualified investments is far too narrow, artificially limiting the availability of qualified investments. **ABA believes that these definitions should be liberalized. As noted above, investments in municipalities' general obligation bonds no longer qualify for CRA credit, as they are not targeted sufficiently towards LMI areas or residents to meet the regulatory requirements. But bank investment in local municipalities' bonds surely is helping to meet the credit needs of the bank's community. However, if the investment test is retained, then ABA strongly recommends considerable liberalization of the definitions. Otherwise there will continue to be a scarcity of qualified investments, making Satisfactory performance under the test unnecessarily difficult, particularly for smaller banks subject to the large bank examination.**

On the issue of whether there is a need for "greater certainty" on how investments will be evaluated in an examination, ABA is cautious of recommending asking for "greater certainty." While all CRA officers want greater certainty in knowing what will be required to get an Outstanding or Satisfactory rating, ABA is concerned that greater certainty means regulations more like quotas, or credit allocation, or adoption of an even narrower definition of what is a qualified investment to achieve that greater certainty. **ABA does not recommend "bright line" tests.**

Service Test Issues

As more banks offer electronic banking and other alternatives to brick-and-mortar branches, they become concerned that the service test depends too heavily on brick-and-mortar branches, slighting electronic delivery of banking services. On the other hand, branches are specifically part of the statute and any new test might pose more problems. **ABA believes that the service test depends too heavily on branches and recommends developing a broader definition of service. ABA strongly opposes a standard considering "not only the delivery method and type of service but also the effectiveness of the delivery method," partly because such a standard would require more data collection and reporting, in order to meet whatever the Agencies might define as the measure of effectiveness.**

The Agencies also ask if the service test is irrelevant to whether an institution is helping meet the credit needs of its community. **While there is no clear statutory authority for the service test, "helping to meet the credit needs of the entire community" would seem to be demonstrated by making branches and other banking services available. Additionally, financial education, particularly education about credit, is sorely needed in the LMI community and should be given credit under CRA. ABA recommends retaining the service test, but modified to recognize an even broader range of services, particularly those related to electronic banking, financial education and other services not tied to brick and mortar branches.**

Community Development Issues

Some large institutions recommend a separate community development test, created by moving the elements of community development from the lending, service and investment tests into the new test. However, establishing a separate community development test does not appear to be statutorily authorized or even contemplated by the Congress. Further, smaller institutions generally see this resulting in added complexity without benefit to them. **ABA does believe that the current regulation's division of community development activities into three separate parts under the lending, service and investment tests does not reflect how banks conduct community development activities. Our banks tell us that community development is a complex and difficult endeavor that is made more difficult and inefficient by these artificial divisions between community development lending, investment and services. ABA believes that the important community development efforts of our banks deserve more recognition than the current CRA regulations provide. ABA would support a separate community development test if there were significant change to the investment test, as discussed above. Otherwise, ABA would retain the *status quo*, as making just this change does not appear likely to result in any overall improvements.**

The Agencies also ask whether the definition of "community development" is appropriate. As ABA has said above, the definition of "qualified investment" is too narrow. This is partly because the definition of "qualified investment" depends in part on the definition of community development, which is itself too narrow. In particular, some bankers find that examiners are requiring that revitalization and stabilization activities occur in low- and moderate-income geographies. Bankers believe that revitalization and stabilization activities contribute to the entire community and so do not need to be restricted to LMI geographies. Further, this requirement creates a problem in non-urban assessment areas that lack explicitly designated low- or moderate-income census tracts or block number areas (BNAs) but which have clear revitalization needs. **ABA recommends that the definition of "community development" be amended to include all revitalization and stabilization activities, irrespective of geography.**

2. Small Institutions: The Streamlined Small Institution Evaluation

There are two issues that ABA believes need to be resolved: (1) the provision creating the holding company affiliation test should be eliminated and (2) the provision setting the asset size for a small bank at $250 million or less should be raised. Under the current regulations, small banks are excluded from using the small bank test if they are owned by a holding company that is greater than $1 billion in banking assets. ABA has always opposed the "holding company affiliate" requirement as not authorized by the statute, which applies only to assessing a bank's or savings association's record of helping to meet the credit needs of its communities. **ABA believes that this provision encourages loss of independence in community banks and is antithetical to the statute's purpose. ABA recommends removing this BHC limitation on the definition of "small bank."**

As to the asset limit on small banks, ABA has long advocated an increase in the size of "small banks." The small bank test clearly confirms or disproves whether a community bank is lending in its community, which is all really that the Act demands that the Agencies evaluate.[2] In 1994, during the last CRA revision, ABA recommended that the small bank limit be $500 million or less. Since the adoption of the revised CRA regulations in 1995, the largest banks have increased their share of total financial assets held by the banking industry, and the range in asset size from a $250 million bank to the largest bank has increased dramatically. It seems incomprehensible that the regulators would class a $250 million bank with a $250 billion bank, but these regulations do. **ABA supports raising the asset size for a small bank to $1 billion, but this should not be at the expense of imposing additional burden on larger banks.**

3. Limited Purpose and Wholesale Institutions: The Community Development Test

The Agencies ask whether the definition of limited purpose should be expanded to a limited extent to capture retail institutions that offer more than a narrow product line on a regional or national basis. **ABA supports liberalization of the community development test, in line with the need for liberalization of qualified investments that compose the investment test, to grant CRA credit for a wider range of investments and services. ABA also supports expansion of the availability to use the community development test for more banks, as suggested by the Agencies. ABA believes that this would give banks greater flexibility under the regulations to demonstrate how they are helping to meet the credit needs of their entire communities. Also, ABA recommends that a limited purpose institution whose principal lending business is other than core CRA loan types (home mortgage, small business or small farm) should be permitted to develop, test and offer lending products outside of the core CRA loan types without jeopardizing their limited purpose designation.**

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2 ABA believes it important to note here that the streamlined small institution evaluation comes closest to what the Congress intended when adopting the Community Reinvestment Act. The Act itself provides that:
"SEC. 804. (a) IN GENERAL.--In connection with its examination of a financial institution, the appropriate Federal financial supervisory agency shall--
(1) assess the institution's record of meeting the credit needs of its entire community, including low- and moderate-income neighborhoods, consistent with the safe and sound operation of such institution;"

Since in 1977 there was only one examination of a financial institution, the safety and soundness examination, it is clear from the statute that the Agencies were to make a general assessment of the institution during that safety and soundness exam. There was no data collection, no paperwork, no separate tests contemplated.

The Agencies also ask if the community development test provides a reasonable and sufficient standard for assessing the CRA record of any other insured depository institutions, including retail institutions. **ABA recommends liberalization of the test, as noted above. Depending on how the Agencies propose to change the community development test, it might be a reasonable and sufficient standard for assessing other institutions, including retail institutions. ABA is interested in seeing additional details from the Agencies on this suggestion.**

4. Strategic Plan

The Agencies ask whether the strategic plan option provides an effective alternative method of evaluation for financial institutions. The Agencies appear to be concerned that the strategic plan has not been used very much, and thus ask if it is a truly effective alternative method of evaluation. ABA supported the creation of the strategic plan option to give banks greater flexibility in helping to meet the credit needs of their communities. **ABA recommends retaining the strategic plan option.**

ABA has asked bankers why they think that the strategic plan is not used very much. Most bankers believe there is a reluctance to use the strategic plan because the Agencies appear to require such a high level of community group involvement and consent before approving a strategic plan. Bankers tell ABA that more banks would use the strategic plan option if community group involvement were significantly reduced. Bankers who have considered adopting a strategic plan have reported that many community groups believe that a strategic plan must somehow benefit them, not just the community. Further, some community groups without any real connection to the communities being considered in the plan nonetheless demand participation in setting of the goals of the strategic plan. **ABA recommends that only community groups actually with a connection to the community have standing to comment on the plan.**

Additionally, bankers tell ABA that some district or regional offices of the Agencies themselves have not been supportive of use of the strategic plan, either by demanding higher performance goals than those to which the bank and the community have agreed or else by strongly discouraging pursuit of the strategic plan option. **ABA recommends that the Agencies review district and regional offices for consistent treatment of institutions considering strategic plans.**

The Agencies ask whether the strategic plan option could be used in conjunction with existing assessment methods for different business lines within one institution, perhaps in the context of a bank with a retail branch network in one part of the country and wholesale operations in another or an Internet presence nationally. **ABA believes that this idea could provide additional flexibility to banks and recommends that the Agencies develop this idea further.**

5. Performance Context

There is considerable concern that the Agencies are not properly judging performance context. Some bankers would like to see a specific requirement that examiners consult with the bank before preparing the performance context. Examiners should also give the bank more information about their analysis and formulation of the performance context. Bankers tell ABA that they do not know how the examiners assess the "performance context," particularly since so many of these performance contexts seem incorrect or inadequate. In addition, bankers often express concern that comparisons made by examiners to "peer" banks in the assessment area are not in fact to peer banks. In part, this is a result of the definition of a small bank being set far too low. This results in

$250 million institutions being classed as peers of $25 billion and larger institutions. **ABA recommends that banks be provided more information by the Agencies on how the performance context is formulated by the examiners. Several bankers recommend a mandatory consultation with the depository institution by examiners before formulation of the performance context. Peer comparisons should be between comparable institutions.**

6. Assessment Areas

Currently, assessment areas are tied to geographies surrounding physical deposit-gathering facilities. Large banks with electronic banking operations and even smaller banks with electronic banking or suburban branches in retail stores are concerned that they are being downgraded for their out-of-market lending. However, many banks are concerned that once the Agencies sever the geographic tie to the assessment area, then new and more problematic bases for the assessment area will cause many more problems. **ABA does not recommend eliminating the geographic/branch basis of the Community Reinvestment Act in delineating the assessment area. ABA suggests that to the extent out-of-market lending is supported by out-of-market deposits, then that lending should be ignored for CRA purposes. ABA acknowledges that banks that want such treatment will need to be able to document at least the amount of out-of-market deposits, but that appears preferable to being downgraded under the lending test. Additionally, ABA supports allowing designation of larger assessment areas, such as regional and statewide areas, instead of just MSAs under the current regulations.**

Some bankers have also reported that examiners expect financial institution assessment areas to be re-configured immediately upon an opening or purchasing a branch in a new geographic area. This requirement not only is burdensome but also, from a practical standpoint, does not afford the institution the opportunity to serve the needs of a community before evaluation of performance. **ABA recommends that either a bank's assessment area should be subject to review and change (if necessary) only on an annual basis or that the performance context for the institution make adjustments for parts of the assessment area that are included for branches operated by the institution for less than one year.**

The Agencies ask if they should create a distinct evaluation method with respect to the assessment area for institutions that gather deposits and deliver products and services without using deposit-taking branches or ATMs, for example, those institutions that use the Internet almost exclusively to gather deposits and deliver products. ABA is concerned that such a new test might lead to new evaluation standards for traditional retail banks without solving any of their concerns. Besides, such institutions already have an option under the strategic plan. **ABA does not recommend creation of a new evaluation method at this time.**

7. Activities of Affiliates that are not Subsidiaries of the Bank

The Agencies ask whether the provisions on affiliate activities that permit consideration of an institution's affiliates' activities at the option of the institution are effective in evaluating the performance of the institution in helping to meet the credit needs of its entire community, and consistent with the CRA statute. **ABA believes that the *status quo* should be retained, allowing depository institutions at their option to request consideration of affiliate activities. ABA believes that this provides the greatest flexibility for institutions and is more consistent with the Act than either mandatory inclusion of affiliate lending or total exclusion of affiliate lending. Mandatory inclusion of affiliates not subsidiaries of the financial institution is**

simply not authorized under the statute, which directs the Agencies to evaluate financial institutions, not holding companies or affiliates of the financial institution. However, allowing financial institutions to include affiliate activities at the option of the institution gives financial institutions greater flexibility under the regulations.

Several bankers report that examiners will not consider the innovativeness or complexity of affiliate activities that the depository institution has requested be considered for CRA credit. **ABA recommends that any affiliate activity being considered for CRA credit be given full consideration for its CRA value, including innovativeness and complexity.**

8. Data Collection and Maintenance of Public Files

First, the data collection is clearly not authorized by the statute or legislative history, as reflected by the fact that the original bill considered by Congressional committee had a data collection requirement that was amended out of the bill prior to enactment. See Appendix 2, below. Second, the data collected is of little use, since it tells little about the actual need for credit by geographical area of the community. Worse, the smaller the depository institution and the fewer small business and small farm loans reported, the greater the unnecessary burden. The few loans reported have no statistical validity to the institution, yet the burden of establishing a reporting system still falls on the institution. **ABA recommends ending the current data collection requirements, as not consistent with the Act. Short of that, ABA recommends that institutions making less than 250 reportable loans be exempt from the data collection. ABA strongly opposes adding any more data collection, because such additional collection and reporting would be burdensome, inconsistent with the statute and of little analytical value.**

9. Other matters

a. Examination Procedures and Examiner Training

Almost every banker with whom ABA has discussed the ANPR has raised the issue of inconsistency in CRA evaluations and in treatment of loans, services and investments by examiners. Bankers see inconsistencies not only among the Agencies but also within the Agencies. While technically not within the scope of the ANPR's questions about the regulations, ABA believes it is impossible to discuss the effectiveness of the regulations in assessing an institution's performance under CRA without considering the training and monitoring of examiners. Examples of inconsistent examinations include participations in loans or common investments receiving CRA credit from one Agency but not from another; conflicting interpretations of community development lending and investment; recognition of accommodation lending by a credit card bank permitted by one agency and criticized by another; different interpretations of HMDA data, and wide variations in formulations of performance contexts within the same market. Bankers report some cases of virtually having to train examiners in the regulations. ABA wrote to the Agencies in 1999 about a very large difference in the percentage of Outstanding ratings given to small banks by the OCC (5% or less) as opposed to the FDIC and the Federal Reserve Board (in the range of 17-21%). The problem for small national banks was so serious that several bankers stated that they would no longer even attempt to earn an Outstanding rating from the OCC. **ABA recommends that the Agencies conduct an annual review of CRA ratings by each Agency to determine if any Agency's ratings distribution varies significantly from the other Agencies. Such variances should be cause for further review as to the reasons for the variation, especially differences in examination procedures and training.**

ABA also recommends that the Agencies conduct surveys of banks recently examined for CRA performance to elicit reports of any problems in the examination, focusing on deficiencies in examiner knowledge, apparent inconsistencies or significant differences of opinion about how the examination was conducted, and the degree of concurrence between bankers and examiners on the results.

Finally, comparison of ratings trends and consistency in examination is made more difficult by apparent differences among the Agencies in dating Public Evaluations and in identifying the examination period. ABA asks the Agencies to adopt a uniform method of reporting a CRA Public Evaluation, including the date the examination commenced, the date the examination ended, the period of operation that was the focus of the examination, and the date the CRA rating was final.

b. CRA Credit for Investments, Loan Participations and Other Ventures in Cooperation with Minority- and Women-Owned Financial Institutions and Low-Income Credit Unions

ABA wishes to raise an additional issue for consideration by the Agencies. The Community Reinvestment Act directs each Agency to assess each institution's record in helping to meet the credit needs of its entire community (12 USC 804(a)). The word "investment" is not used in the Community Reinvestment Act except in one place. In Section 804(b), the Community Reinvestment Act specifically authorizes each Agency to "consider as a factor capital investment, loan participation, and other ventures undertaken by the [majority-owned] institution in cooperation with minority- and women-owned financial institutions and low-income credit unions provided that these activities help meet the credit needs of local communities in which such institutions and credit unions are chartered." The Agencies have never adopted any regulations granting CRA credit for such investments, participations and other ventures, thought ABA has been told that Agencies have occasionally given CRA credit on an *ad hoc* basis to individual institutions. ABA believes that the Agencies have done a disservice to minority- and women-owned institutions and low-income credit unions by failing to implement this authority. ABA requests that the Agencies issue regulations so implementing this unused authority.

ABA notes that this provision of the statute has only one geographical restriction: that the "activity" help meet the credit needs of the minority- or women-owned institution's community. The statute makes no reference to the community of the majority-owned institution, so that such investing institutions could be given CRA credit for these specific investments, even though they might be outside of the institution's assessment area. ABA is aware that the Agencies have given CRA credit for investments in minority- and women-owned institutions on a case-by-case basis, but apparently these specific investments have never been in institutions outside of the investing institution's assessment area (community). **ABA recommends that the Agencies provide that such investments, participations and other ventures result in CRA credit to the majority-owned institution without regard to the location of the minority- or women-owned institution or low-income credit union. Further, ABA recommends that grants for professional development and training of personnel of a minority- or women-owned institution or low-income credit union should count as either capital investment in the institution or as a credit-related service.**[3]

[3] ABA helped organize and supports the Minbanc Foundation, Inc., an education foundation that provides grants and training materials and courses to minority-owned banks. ABA has previously petitioned the Agencies to grant CRA credit for financial institutions' investments in the Minbanc Foundation, Inc. See letter from the ABA to the Agencies dated October 14, 1999. Under current CRA regulations and interpretations, such investments do not qualify for CRA credit for the investing majority-owned institutions.

Conclusion

The American Bankers Association appreciates the opportunity to comment on the Agencies' Advance Notice of Proposed Rulemaking on a possible revision of the Community Reinvestment Act regulations. ABA notes that the questions raised by the Agencies are complex, and on several of them there does not appear to be complete consensus in the industry on the appropriate answers. ABA's recommendations are intended to make the regulations more closely follow the statute than they currently do and to give banks and savings associations more flexibility in demonstrating that they are helping to meet the credit needs of the entire communities in which they are chartered. If there are any questions about these comments, please call the undersigned at 202/663-5331.

Sincerely,

Paul Alan Smith

Paul A. Smith

APPENDIX 1.

The Investment Test Is Not Authorized By The Community Reinvestment Act

The Community Reinvestment Act mandates that the Agencies evaluate the record of financial institutions in helping to meet the credit needs of their entire communities in which they are chartered. It says nothing about evaluating financial institutions' investment, charitable contributions or public service grants. In fact, the only reference in the Community Reinvestment Act with regard to investments by insured depository institutions is a grant of authority for banking regulators to factor into the examination any investment by "majority-owned institutions" undertaken in cooperation with "minority- and women-owned financial institutions and low-income credit unions." This section of the law was enacted by Congress to authorize CRA credit for investments because Congress was concerned that the Agencies would not otherwise be able to give CRA credit for such investments under the original terms of the Act. It is clear from this that Congress did not intend any "investment" requirement for the Community Reinvestment Act, and the Agencies' addition of a general "investment test" component of the CRA rating is not statutorily authorized.

As we said in our comment letter of November 21, 1994, on the proposed revision of the Community Reinvestment Act regulations, we believe that the regulators had exceeded the Act in their proposal of investment test and service test components and a ratings matrix as part of the large bank CRA performance evaluation.

> "A key problem with the ratings system is that there appears to have been a shift in the level of required performance under the CRA that has not been mandated or clearly discussed. The basis of CRA is the extension of credit, specifically the institution's record of helping to meet the credit needs of its community. There is no mention of regulatory evaluation of "service" or "investment" in the statute. The current proposal recognizes the primacy of lending by providing that no institution can receive a composite rating score higher than twice its lending test score. Nonetheless, the regulators provide in the ratings system that a bank that is doing an adequate job in lending to its community may be rated as "needs to improve". For example, a bank doing an adequate job lending would receive a "low satisfactory" for lending or 6 points. If an examiner then concludes that the bank deserves a service test rating of "needs to improve," perhaps because demographic shifts have occurred in its community and the bank has not added branches to meet all of those shifts, the bank would get 1 point for service. If the bank was concentrating on lending and thus did not believe that it needed investments to offset a poor lending performance, then the bank would probably be rated a "needs to improve" for investments, getting another point. Then the bank now has 8 points and gets a final rating of "needs to improve," although it is doing an adequate job lending in its community. ABA thinks this is an improper and unacceptable result under the statute. ABA strongly recommends that the regulators need to return to the first proposal, in which a bank's service and investment rating could improve a lending score but could not reduce a satisfactory lending record to a less than satisfactory rating. [P. 11, emphasis added.]"

APPENDIX 2

The Requirement for Small Business and Small Farm Lending Data Collection and Reporting is Inconsistent with the Community Reinvestment Act

The Community Reinvestment Act is silent on requiring the collection and reporting of any data. This silence is because the original reporting requirements were amended out of the legislation. However, the Agencies have concluded that this silence is grounds for them to impose data collection and reporting requirements that the Congress actually considered and refused to impose. However, the legislative history clearly demonstrates that the Community Reinvestment Act does not authorize imposing any additional data collection. ABA believes that it is worth repeating the words of the Committee report[1]:

> "The question of whether the bill will increase the regulatory burden on financial institutions was thoroughly considered by the committee. The committee believes that the regulatory agencies already have sufficient data available to carry out the intent of this act without requiring additional red tape.
>
> "As originally introduced, S. 406 would have required the filing of certain additional material. The Committee was informed that substantial data is already filed in connection with both charter applications and applications for new deposit facilities, and after a full discussion, concluded that these additional reporting burdens would not be necessary or appropriate to the enforcement of this Title.
>
> "Loan files are already available to examiners in periodic examinations of financial institutions. These files, of course, indicate where loans are made. They will reveal whether a disproportionate amount of credit is being provided outside of the institution's local territory. The Equal Credit Opportunity Act, as implemented under Regulation B, requires that loan applications be retained, and these will provide one indication of local loan demand. The ability of competing institutions to find loan opportunities locally also reflects local credit demand."

The agencies state that the data collection is validly imposed under the Community Reinvestment Act. ABA believes that this misstates the law. While the statute authorizes the agencies to issue implementing regulations, those regulations must comport with the purposes of the statute. As evidenced by the legislative history, the purposes of the statute were not to require further reporting but rather to compel the agencies to do a better job under existing legislation. To quote the Committee Report: "The Committee believes that existing law provides general authority for the financial supervisory agencies to emphasize to institutions that their main obligation is to their primary service areas. The need for new legislation arises because regulating agencies lack systematic, affirmative programs to encourage lenders to give priority to the credit needs of their home areas." As noted earlier, Congress concluded that no additional reporting by financial institutions was necessary. To the contrary, additional reporting requirements were removed from the legislation in order to obtain passage of the bill. The removal of these reporting requirements demonstrates that the "purposes" of the statute do not include creating additional reporting burdens. Therefore, regulations authorized in the statute to effectuate the purposes of the statute <u>cannot</u> impose additional reporting requirements that were clearly not within the purposes of the statute.

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[1] "Joint Explanatory Statement of the Committee of Conference", <u>Compilation of the Housing And Community Development Act Of 1977</u>, October 1977, p. 65