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October 17, 2001

Regulation Comments
Chief Counsel's Office
Office of Thrift Supervision
1700 G Street, NW
Washington, D.C. 20552

Attention: Community Reinvestment Act Regulations
Docket No. 2001-49

Dear Sir or Madam:

As part of an interagency effort to elicit the views of industry management concerning the "Joint Advance Notice of Proposed Rulemaking" regarding the Community Reinvestment Act (CRA), I joined with personnel from the Kansas City and Minneapolis Federal Reserve Banks and the FDIC to hold focus group meetings. The meetings were held in Denver, Colorado; Kearney, Nebraska; and Pierre, South Dakota.

We were attempting to discern the special problems that these institutions might confront in managing their CRA operations in different types of lending areas. We wanted to obtain comments regarding the CRA regulations and their impact in serving "high cost" areas, rural communities and those in which Indian reservations are located. We found that in many respects the institution managers had similar concerns.

I have attached comments received at each of these meetings as well as a list of the participants at each of the respective meetings. If there are any questions concerning these comments please contact me, Dave Whittaker, through my regional office at (972) 277-9567.

Sincerely,

/s/Dave Whittaker
Compliance Examiner

Enclosures

CRA Focus Group
High Cost Areas
Denver
September 14, 2001

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Attendees:

Tracy Stanfield – Alpine Bank
Glenn Smith – Wells Fargo
Linda Tinney – US Bank
David Kelly – FirstBank
Karen Hennessy – WestStar
Michael Martinez – Vectra
Veronica Ware – Commercial Federal*
Anne Lovett – Citywide Financial

Ariel Cisneros – FRB
Andrew Thompson – FRB
Jeni McCormick – FRB

* OTS regulated entity

OTS personnel were not able to attend due to travel problems caused by the September 11th attacks in New York City.

To Change or Not to Change?

In summary, every banker at this session voiced the opinion that the regulation should not be overhauled. The bankers believe that the CRA works well as is, although they provided several suggestions for minor revisions.

Performance Context

The bankers saw the performance context as the single most important piece of a valid CRA assessment.

Many were dissatisfied with the level of understanding that examiners have of their performance context, or their willingness to view certain performance issues through that context.

Performance context issues can vary dramatically from one area to another (Aspen/Vail "high cost/income" vs. Cedaredge/Delta "mixed income"). These differences are not so marked usually moving from one MSA area to another. There are greater differences between rural areas being compared than there are in MSAs.

Larger banks with presence in higher population areas have little incentive to worry about CRA in high cost or rural areas where they may have branches. The examination, due to performance context issues, will be driven primarily by the MSA considerations.

There was some discussion regarding allowing the performance context to define the "weights" given to lending, investments, and services. (i.e. – if there are no investments available in an area then allow a greater weight to be placed on one of the other factors) However, several bankers were uncomfortable with the added subjectivity this would introduce.

Community Development

The bankers suggested that community development (CD) may be weighted too heavily and that certain CD provisions should be modified. There was not an overwhelming feeling that the actual definition of community development be broadened.

Performance context issues are critical in community development assessments in high cost areas. For example, moderate-income homes in these areas can reach $350,000. The bankers felt that there was an over-reliance on HUD-generated income figures in the CRA analysis to the exclusion of performance context issues.

Similarly, there seemed to be support for fitting CD limits into the definitions set up by the communities. For example, if someone qualifies for deed restricted housing, even though the cost may seem more than a low-mod person might be able to afford, these should count toward community development.

The banks were frustrated by what they see as excessive documentation requirements to prove that an activity meets the CD definition.

CD Loans:

The bankers believe that the current regulation inaccurately captures their CD lending efforts by capturing them first in other applicable areas. This is most common in the non-Metro banks where there are limited community development lending opportunities. There was the feeling that the "double-counting" exception for multifamily housing should be expanded to single-family homes and to small business loans. As an alternative to double counting, the bankers suggested that they should be able to classify these loans as CD loans instead of the default (HMDA or small business) or as either based on their choice.

The bankers felt that their efforts in providing loans (and investments and services) to employees of businesses in high cost areas do not get sufficient credit. Some consideration on an economic development level is warranted because the businesses wouldn't otherwise be able to exist.

The banks expressed concern that loans to employees (who would be considered low or mod-income) in high cost areas actually count against them because in the areas where these workers reside, they are often middle-income earners.

The bankers stated that there is a difference between employee housing (which community leaders and the banks agree is a huge need) and low-mod housing (which doesn't exist and isn't really allowed to exist.) Areas such as Vail have not allowed moderately priced housing to start in that area. Most Vail workers live in areas such as Cedaredge. They feel that the regulation should allow for consideration of employee housing in these areas, rather than focusing more exclusively on low-mod housing.

In high-cost areas, the primary purpose test often fails with regard to employee housing. Usually these communities require the provision of employee housing as part of the approval for other development. For example, if a developer is building 10 market-priced units, the municipality may require that they also add 4 employee-housing units. While critical to the economic health of the area, these efforts go uncounted as far as CRA efforts because they fail the primary purpose test.

More distinction should be made between low-income borrowers and those who are under the poverty level. The bankers felt that they were often held to match the low-income ratios exactly, even though this wouldn't make sense from a safety and soundness perspective.

Much of the lending activity in these banks is consumer related. However, even when they collect data and ask for it to be considered, the bankers felt that this area receives little consideration.

The bankers wanted to see CD loans included on the FFIEC disclosure statements. Specifically, the disclosure statements now only include summary data with no geo-coding information.

CD Investments:

There is no infrastructure in many non-Metro areas to make community development investments possible.

As with CD services, in small communities, the institutions have an extraordinary amount of competition with other banks to divvy up the pieces of an often-small pie. "Community banks are tripping over each other trying to get the limited opportunities."

Because of the limited investment opportunities in many non-Metro areas, the bankers suggested adding additional flexibility to the regulation in those circumstances. They suggested even adding alternative activities that banks might engage in that would help offset the lack of investment activity. They also suggested "credit" for trying, or some baseline rating, if no opportunities exist.

Recommendation made to strike the criteria for "innovative and flexible." The bankers felt that often the community needs can be at least as well met if not better met by simple straightforward investments. Additionally, there is considerable subjectivity in determining what is innovative or flexible. For example, something may be innovative and complex for one institution, but not for others.

CD Services:

It is difficult to find services that are "targeted" to low-mod people in many small communities. If the community sees a need for a service, it is most often open to anyone in the community.

In non-Metro communities, the assistance of non-profit partners is limited. Therefore, it is more important to provide the actual services than to give money to someone else to do it. However, because these services are often not related to the banker's financial expertise, these activities receive no credit.

One banker recommended de-emphasizing branch openings and general branch locations since so many alternative delivery methods are now available.

The bankers felt that affordable housing grants should be given more credit than simply as a CD service. They stated that these grants take considerable time and energy. One banker mentioned that the FHLB is finding few participants in this program because of the large investments of time coupled with very low CRA return.

Data Collection

Some alternative should be developed for dealing with PO addresses in rural areas. There are often no physical street addresses available.

Examination Process

The bankers feel that examiners, in general, need to have more expertise in high cost/rural/Indian country issues. They hinted at having "specialists" for these areas that could provide more performance context implications to the overall exam.

Some of the bankers condoned adding more specific guidance to examiners in the exam procedures, rather than in the regulation, regarding banks that do not fit the "typical" mold.

The bankers were frustrated by the unofficial ratios used by the OCC in determining ratings. They feel that if ratios are to be used (which they generally did not advocate) they need to be formalized.

The bankers felt it was unfair to limit the number of "outstanding" institutions just because a "quota" had already been filled.

For banks with multiple assessment areas, the bankers thought that an overall weighting of specific areas (which they said is what examiners typically do) contradicts performance context issues.

The bankers felt that uniform application of the CRA regulation to all banks regardless of regulatory agency is currently lacking.

One banker suggested that the regulatory agencies should have more information about what investments are available rather than relying on the bank and community contacts to supply this information.

Other Recommendations

Eliminate the requirement to have CRA files in all locations. While there is very low usage of these files by the public, the administration and maintenance on these files (not to mention supply costs) is a resource drain. The banker recommended having one copy maintained at a given location with the requirement that all requested documents be sent to any requester within a given time frame via a choice of delivery options.

FFIEC should "do" the performance context for each market and then get the buyoff of the local banks.

Other industries should be subject to CRA requirements as they are in direct competition with banks.

The bankers felt strongly that letters of credit should receive CRA consideration. They mentioned specifically, how important these letters are in the realm of community development lending. They also indicated that this was of major significance in high cost areas, particularly. (LOCs actually are permitted in some instances.)

The bankers recommended that automated underwriting concerns should be addressed as it becomes more commonplace. Specifically, the bankers expressed concern over the collection of revenue and personal income. They feel that automatically excluding these loans from consideration would skew their actual performance, yet they feel that collecting this revenue and income information works against the cost efficiencies of credit scoring.

One banker recommended changing the baseline of non-Metro state median income to county income. This would make the analysis more reflective of the bank's actual assessment area and would preclude the requirement for banks in high cost areas from keeping two sets of data; one for non-Metro to track actual performance and another from county to explain performance context.

One banker suggested that the strategic plan option leaves too much uncertainty for the bank with a 3 to 5 year window. Another suggested that this evaluation method should be eliminated.

CRA Focus Group
Rural Areas
Kearney
September 17, 2001

Attendees:

Robert Hallstrom – Nebraska Bankers Association (NBA)
George Beattie - NBA
Joanne Holmes –Equitable FSB*
Mark Thomas – Platte Valley State Bank & Trust
Dick Allinger – Bank of Bennington
Arlen Osterbuhr – Minden Exchange Bank
Leo Kringle – Sherman County Bank
Cliff Keslar – Ravenna Bank
Jim Varney – Custer Federal S&L*
Richard McGinnis – Home Federal S&L*
Larry Bottger – First Nebraska Bank - Valley
Cindy Nieves – Commercial Federal Bank*
Leslie Anderson – Bank of Bennington / NBA

* OTS regulated entity

Jay Shellburg – FDIC
Kevin Shields - FDIC
Dave Whittaker - OTS
Larry Meeker - FRB
Andrew Thompson - FRB
Jeni McCormick - FRB

To Change or Not to Change?

In summary, the bankers at this session voiced the opinion that the regulation should not be overhauled. However, the bankers believe that there should be some substantial changes regarding the small bank definition. In addition, there was discussion about the elimination of the investment test (for both small and large banks.)

The bankers expressed the sentiment that changes are inherently burdensome, even when those changes would improve the system. With that in mind, they were cautious of making suggestions for changes that might cause increased burden.

The bankers suggested that although there are some "rumblings" of dissatisfaction with the current regulation, these are nothing like the comments heard prior to the 1995 changes.

Small Bank Definition

The bankers generally believe that "small," rural banks should not be subject to the CRA regulation. However, they understand that there will be little support for that position and, therefore, recommended changes to the small bank definition.

A $1 billion threshold was mentioned several times as a more appropriate assets size threshold. The bankers indicated that they would be pleased with any relief, even if it was only a $500,000 threshold. The overall sentiment was "the higher, the better."

The bankers feel that the $250 million threshold is inappropriate. They stated that they feel that this threshold was NEVER appropriate, not simply that the growth in bank assets requires a change from the 1995 threshold.

The bankers also expressed that whatever asset threshold is determined, consideration should be given to making it adjustable, and not static as of the date of the regulation's change.

The bankers also voiced support of an MSA vs. nonMSA distinction for small banks. According to this discussion, there might be differing asset size thresholds for small banks inside of MSA than those outside of MSAs. Another option discussed was considering any bank outside of an MSA as a small bank.

The bankers also discussed the possibility of creating an "ultra small" institution designation that would either be exempt or subject to "super-streamlined" exams. An "ultra small" institution could be defined by a given asset size, outside of an MSA, and in a "red zone" portion of the country. (These "red zone" areas are from USDA maps dealing with rural area demographics and are areas in which population or income growth was below the national average.) The "super-streamlined" exams could be simply an offsite analysis of the bank's loan-to-deposit ratio and its loan portfolio.

The bankers suggested that the holding company size should not be a factor in determining whether a bank is small. They stated that particularly in the investment realm, the rural community banks have the same basic constraints and opportunities, regardless of their holding company size.

Rating Categories

The bankers stated that community banks take a considerable amount of pride in the involvement that they have in improving their communities. This pride is generally what drives a community banker from being satisfied with a satisfactory rating and going to the additional work to achieve an outstanding rating.

The suggestion to eliminate the "outstanding" rating was raised. The sentiment was that rural bankers are going to do what they are going to do; regardless of what they get credit for.

There was discussion regarding those banks that are not meeting the requirements of the CRA and how those institution's actions affect their communities. The general sentiment was that there are few, if any, underserved markets in rural America. Any opportunities made available by poor performing banks are quickly absorbed by nearby competition. This discussion gave way to a sentiment that "if the good bank's are doing what they can, and the "bad" banks aren't hurting their communities, why does there need to be so much regulatory burden on the good banks?" This discussion may provide grounds for recommending higher thresholds for the small bank definition.

Investment and Service Tests

There were differing views regarding qualified investments and services. Some bankers suggested that changes would inherently add burden to compliance with the regulation. Other bankers suggested that they are not given credit for the types of investments and services that are truly needed in their communities due to the strict interpretations.

The sentiment was also raised that investments do not help to meet the credit needs of communities and, therefore, the investment test should not be included in CRA. Further, some bankers felt that the regulators lacked the statutory authority to include investment tests in the regulation.

Some bankers suggested that the large bank test should be revised to mirror the small bank lending test. They felt that services and loans are inseparable and that the investment test shouldn't be a factor anyhow.

Some attendees suggested that regulators "interpret" investments as an enhancement opportunity…not as a downgrade. There was the perception among some attendees that regulators downgrade even small banks for lack of investments.

The bankers felt that in many small communities there is a leadership void that the bankers are critical to filling. The bankers indicated that these activities are often the driving forces in community enhancements. There were mixed feelings, however, between those bankers who wanted to be given credit for such things as Rotary or 4H involvement and those who did not want to have to document this involvement.

The bankers indicated that simply by the types of people they hire, they are contributing to their communities in significant ways. Specifically, they indicated that hiring decisions in rural banks are largely dependent on the willingness of the applicants to become a viable part of the community, outside of the bank.

To help minimize burden and increase interagency consistency, the suggestion was raised for the regulators to develop a list of "acceptable" investments. (Consumer credit counseling was an example given.)

Loan to Deposit Ratios

The bankers expressed concern that their deposits are so rate sensitive.

One banker was concerned that the LTD only measures one aspect of an institution's balance sheet. He thought that the regulators should consider the change in structure to the balance sheet when banks are involved in insurance and investments.

Performance Context Issues

Many small rural banks have no low- or moderate-income geographies in their assessment areas. While they feel that examiners may give some consideration to credit extended in "blighted" areas, the competition for these loans is fierce. The small banks are often unable to compete with the large institutions for this business.

The rural banks are particularly concerned about the age demographics in their assessment areas. They stated that their agricultural customers are aging and that any viable ones are being picked off by agencies such as the Farm Services Agency. The Farm Services Agency generally tries to select only the best customers, leaving the rest for the area banks.

Data Collection

Changes in the data collection rules are incredibly burdensome to "small" large banks. (The change with the reporting of renewals was specifically cited. Additionally, the banker said that changes in "interpretation" were often just as problematic.) The bankers had heard some mention of additional reporting requirements, including race or gender data, and were very much opposed.

The bankers felt that gross revenue documentation is fairly burdensome, as this is not a piece of information routinely collected by the banks for other business reasons. They felt that net income would be a less burdensome piece of information to collect.

There was sentiment that the time that the smaller large banks spend doing data collection could be better spent in ways that would actually benefit the community.

Other Recommendations and Comments

Eliminate the requirement for maintaining a public file. The bankers reason that only examiners request the information and the most critical pieces of information are available through alternative sources. The amount of time devoted to maintaining the files is not worth the value.

The bankers felt that there are so many alternative sources to credit out there, that they are often left to ultimately meet the needs of the least qualified members of their communities. The bankers cited the Farm Service Agency, in particular, as one who "cherry picks" the best customers. The bankers also mentioned dealer credit, insurance and investment firms.

The banks expressed concern about the economic viability about some of their communities. They indicated that they are placing much effort into economic development, but form over substance still seems to prevail in the CRA view of the things they do.

One banker stated that marketing and community involvement are key pieces that are missing in the current regulation. However, other opinions countered saying that they do these things as good business practices, not in order to get CRA credit. These bankers felt that gathering information and spending time figuring out what "counts" could be spent more productively elsewhere.

The bankers discussed the fact that large, regional institutions with branches in rural communities are not completely prevented by the CRA from pulling local deposits and using the funds elsewhere. They felt that this was a result of too much weight given to the higher population areas. (Other bankers mentioned that this may also sometime occur with small banks with several branch locations.)

The Internet was not of major concern to the bankers at this session. They indicated that it is generally not a large part of their business and rarely would affect their in/out percentages or any other CRA factor.

The bankers were generally against adding any hard ratios or benchmarks into the regulation. They indicated that the performance context is critical in many small institutions.

CRA Focus Group
Indian Country
Pierre
September 19, 2001

Attendees:

Diana Fister – Dacotah Bank
Keith Willard – 1st Financial Bank
Trent Sorbe – 1st Financial Bank
Bruce Haerter – Farmers State Bank
Ed Kentch – First National Bank
Mike Zimmerman – Home Federal Savings*
Boyd Hopkins - CoreTrust Bank
Bob Clair - American State Bank
Mary Kay Carter – American State Bank
Chandra Love – American State Bank
Tom Adam – Dakota State Bank

* OTS regulated entity

Donald Spiers – FDIC
Kevin Shields – FDIC
Dave Whittaker – OTS
Mike Wold – FRB
Andrew Thompson – FRB
Larry Meeker – FRB

Indian Country Issues

Many loans in Indian Country are so small they cost more than the bankers earn. However, they are not large enough to make a significant difference in lending volume. Hence, the loan to deposit ratio does not accurately capture performance. This also makes an "outstanding" rating virtually impossible for many small banks. The lending performance test should consider more than simply the dollar volume.

The regulation does not take into consideration the uniqueness of Indian Country. Specifically, the unique governments and separate treaties, the fact that governing bodies change often and the cultural issues that add to the challenge.

Indian Country needs job creation. It is important to encourage big businesses to locate there. However, there is lots of risk in lending to companies that can provide jobs, but banks often don't get CRA credit because the owners are upper-income.

Helping tribes to form their own banks may be a better alternative than forcing other banks to meet credit needs because tribes are more familiar with their culture.

Small Bank Definition

Small bank limits should be raised to $1 billion.

The bank holding company test should be eliminated due to the fact that there are few investment opportunities even for large banks operating in small rural communities. Even a $10 billion bank in this area feels like a small bank.

A $250 million bank and a $250 billion dollar bank should not go through the same CRA exam. The bar needs to be able to "float" more easily. This may be accomplished through performance context factors.

Some measurement of functionality should be included in the definition, rather than strictly an asset-size test.

There was a suggestion to index the small bank size cut-off.

Rating Issues

The desire for higher ratings is driven by being in an acquisition mode.

Bad CRA performers are causing more stringent requirements for the good performers. The market punishes the poor performers without impacting the community adversely. Credit needs are being met (as can be seen by statistics that show that credit is too plentiful). Additionally, competition is fierce and will naturally fill the voids (including Internet, Farm Credit Services, etc.).

Investment and Service Tests

Some of the bankers expressed that the investment test should be discarded, as it is meaningless. Some thought, however, that the service test should remain. Others thought that both should be eliminated and that community banks should be evaluated only under a lending test.

The bankers expressed an interest in having more of the things they do for the community as a whole to be included in the CRA evaluation.

The strict interpretation of low- and moderate-income areas should be eliminated in sparsely populated areas. (For example, when buying bonds for a rural volunteer fire department, the 51% LMI test should not apply.)

Large banks (e.g. CitiBank) throw large dollars into investments, which raises the expectations for the local lenders. But the small banks are the primary lenders. The very large banks can outbid small banks because they are required to have investments as part of their CRA.

Large banks make investments in MSAs or statewide entities where they get credit. They are much more lax in rural areas since their exam generally focuses on metro area performance.

SBICs and other investment opportunities often don't help the local community. However, there is pressure to make those investments.

Performance Context Issues

The bankers stated that viability is the key issue for both rural communities and rural community banks.

Performance context cannot be accurately judged in a few days in the community.

Data Collection

The bankers would like to see a moratorium on data collection. In that absence, some felt that subsidies should be made for future changes.

These bankers do not want increased data collection requirements for such items as race, gender, etc.

"There is nothing worse than a data integrity scrub by the regulators."

Public File

The public file requirements should be eliminated. They are burdensome to maintain and are only rarely requested. Key information is more readily available from other sources. These other sources include the web, the bank's own website, service brochures, etc.

Some items that were thought to be useful public file information include:

- Assessment area maps
- CRA complaint letters

The bankers saw no reason to keep a file at every branch.

Bankers suggested that more extensive file requirements might be required for banks with a less than satisfactory rating. However, they still doubted its usefulness.

Other Recommendations and Comments

Whatever happens, these bankers hope that no additional regulatory burden is placed on small banks.

"Our bank was CRA before there was a CRA."

"CRA puts a gun to the banker's head."

The bankers stated that there is a lack of consistency on the lending, investment, and service tests.

Other competitors, such as Farm Credit Services, should be subject to the same requirements.

The "Sunshine Provisions" should be repealed.

Expectations for small banks are not always realistic. There is a tone of banks needing to <u>prove</u> that they are meeting credit needs vs. the examiners <u>assessing</u> that effort.

Fair lending is a huge part of the CRA. If you've done well on fair lending, you must be doing well on CRA.

Don't bring predatory lending issues into CRA compliance.

The Privacy Act is costing a tremendous amount of money.

In sparsely populated Non-MSA areas, the focus on LMI areas and individuals should be thrown out the door.

The Community Development Test is not well defined...If it is good for the community, it should count for CRA.

Community Development should be broadened to include anything that a bank does if it is good for the local community.

Local communities need services that are not directly related to the availability of credit. Banks should be encouraged and rewarded for providing leadership and needed services.