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Dear Sirs:

We understand that the bank regulatory agencies have begun consideration of revisions to the 1995 CRA regulations and that you intend to issue an Advanced Notice for Public Rulemaking (ANPR) later this year.

In general, the 1995 regulations were a major improvement over the prior regulations. The changed emphasis in CRA examinations from process to outcomes was a critical shift and has resulted in much more substantive examinations and the development of concrete expectations for bank performance. The tripartite division of the examinations into lending, investment, and service tests allows concentration on key elements of bank activity. These basic structures of the 1995 regulations have proven their worth and should be maintained.

As the Woodstock Institute has worked to promote community reinvestment under the structure of the 1995 changes, we have noticed, however, that several key provisions have hindered rather than helped that goal. As you

frame the ANPR, we request that you consider the following modifications that we believe would produce a more effective rule.

### **Definitions**

**1. Community development loans:** SBA guaranteed loans or SBIC loans should not be given automatic coverage. Those loans should only count if they go to a business in an LMI or minority tract or to a minority owned firm. [228.12 (i)]

**2. Home mortgage loan:** The definition should include all home-secured loans. Loans for different purposes (e.g., purchase, refinance, and home equity) should be counted separately. [228.12 (m)]

**3. Wholesale or limited purpose bank:** These definitions are too broad. A bank should be considered a retail bank if a significant share of its lending is retail (housing, small business, or consumer) OR if its market share in any product in any MSA or county is above 0.5 percent.

### **Lending Test**

**1. Originations should be considered primary products and purchases secondary products.** The numbers should be the most important criteria, then the quality, including price and terms. [228.22 (c)] Originations should be given more credit than purchases and the two channels should be considered separately.

**2. Geographic distribution criteria should include race of neighborhood.** There is a precedent for this in the investment test, which gives credit for making a branch available to a minority or women-owned depository. [228.22 (b)(2)] Moreover, the CRA statute provides that the bank examiners assess an institution's record of meeting the credit needs of the entire community. [12 USC 2901 s. 804 (1)] Given the racial disparities in lending patterns, the CRA regulations should contain an explicit reference to distribution of loans by race.

**3. Community development lending:** The criteria for community development lending should include responsiveness to community development and credit needs. [228.22 (b)(4)]

**4. Affiliates' lending should always be reviewed.** The provision that affiliate lending should only be examined at the bank's option should be removed.

[228.22 (c)] Under no circumstances should a bank have the choice of having affiliate lending examined. The current regulation merely encourages financial institutions to distribute loans between the bank and mortgage affiliates to make bank lending practices look better than the financial institution's aggregate lending practices.

**5. The origination or purchase of predatory mortgage loans:** The regulation should provide that if any lender violates any federal or state consumer lending law, then that institution's grade in the lending test would be downgraded. Examiners should inspect an institution's geographic market share ratios (by income and race) for both prime and subprime lending and compare those ratios to the institution's competitors in the same market segments.

**6. Predatory consumer loans:** Financial institutions that provide or fund other institutions to provide predatory consumer loans (such as payday or vehicle title loans) should receive negative points for providing them. Similarly, any lender that violates any federal or state consumer lending law should be downgraded.

### **Investment Test**

**1. Investments in lower-income communities** are vital to the economic vitality of those communities. This test should be retained as a separate test.

**2. All affiliate investment activity should be considered.** [ 228.23 (c)]

**3. Broadly different types of investment should be evaluated separately** e.g. grants vs. deposits, high return/low risk, low return/high risk. A high rate of return investment in an untargeted SBIC, for example, should not be considered equivalent to a similarly sized, lower return investment in a CDFI that lends to hard-to-finance projects in a low-income community.

**4. Each category of investment should be measured relative to a bank's equity capital** (or tier 1 capital). Grants should be measured relative to a bank's earnings. For banks with multiple assessment areas, these ratios should be calculated from a prorated share of equity or earnings based on geographical share of deposits.

## Service Test

- 1. The provision of basic retail banking services is critical** to the financial health of low-income people. The test should be retained as a separate test.
- 2. The service test should be applied to all institutions** that provide retail banking services, however those services are delivered. In the CRA examination process, emphasis should be placed on brick and mortar branches because of the benefits they bring to a community.
- 3. Currently, examiners are required to consider the current distribution of branches** and in the context of that distribution, the bank's record of opening and closing branches. [228.24 (d) (1 and 2) Special weight should be given to the current distribution of branches because the more recent record of opening and closing might well conceal an inadequate initial distribution.
- 4. Data on account holders.** Examiners should consider distribution of retail banking accounts by income, race and geography. The CRA statute expressly includes deposit services in the definition of convenience and needs. [S. 802 (a) (2)]

## Ratings

- 1. The final ratings should be expanded to five categories including high and low satisfactory.** [228.28(a)] The current provision of four categories encourages grade inflation.
- 2. No bank should receive a satisfactory rating if it receives a substantial noncompliance rating** on any component test or if it receives a needs to improve rating on more than one component test. [228.28, (b)(3)] No bank should receive an outstanding rating if it receives either a SNC or an NTI rating on any component test. [228.28 (b)(1)]

## Assessment Area Delineation

- 1. A bank's delineation of its assessment area should be evaluated by the Board.** We are finding too many examples of assessment areas that disregard the requirements described in the 1995 regulation. [228.41 (a)]
- 2. The assessment areas of many limited purpose financial institutions are a sham:** FSBs operating through insurance agents, credit card banks, and Internet banks regularly and intentionally do the vast majority of their banking

business outside the MSAs in which their headquarters are located. Yet these institutions have been permitted to limit their assessment areas to their headquarters' MSAs. The archaic interpretation of the CRA regulations that tie assessment areas to areas around branches undermines the intent of the statute. The geographical unit of assessment should generally be no smaller than MSAs or counties. A financial institution should include the following in its definition of its assessment area:

(a) MSAs or counties where it has branches and ATMs

(b) and any MSA or non-metro county where it has originated a significant portion of its loans (e.g., 0.5 percent).

(c) and any MSA or non-metro county where it has originated a significant portion of the total loans made in those geographies in the most recent year (e.g., 0.5 percent).

(d) adjustments to these areas to include only a portion of an MSA or county should be limited to those institutions with less than \$100 million in deposits in the MSA or county.

**3. When a bank with multiple charters in a single MSA is examined,** analyses should be based on performance within the entire MSA rather than on the specific assessment areas delineated by the bank for the specific charter. The smaller assessment areas for specific charters in a single MSA may skew the performance of the bank relative to the entire MSA performance.

### **Strategic Plan**

**1. The strategic plan option should be rescinded.** Very few institutions use the option. In situations where it is used, Woodstock Institute analyses show that the measurable goals that financial institutions set for themselves are far too low by a variety of measures. The institutions and the examiners pay little attention to community comment on those goals. [228.27]

### **Data**

**1. Small business data collection should mirror HMDA provisions** and include data on each application, the race and gender of applicants, as well as the industry, annual sales, loan size and disposition of the application. The institution should also provide the reason for loan denials and the interest rate

and terms of loans originated. [228.42] These data should be fully disclosed to the public as is HMDA data. The current form of the public data is intentionally designed to limit its utility to community groups.

**2. The 2001 procedures for filing that permitted one small business refinance or renewal** made within a year of the original loan to be counted as an additional loan should be rescinded. This provision gives institutions a perverse incentive to make short-term rather than long-term loans to get credit for more “originations”. Any reporting of renewals or refinances should be done separately. These are different products with different utilities.

**3. Community development lending data should be more detailed and consistent.** It should follow the LAR format with information on the purpose of the loan (housing, business development etc.) and the dollar volume of each loan.

**4. Institutions should provide data on account holders.** This data should include income, race, location (census tract where account holder lives), average balance, type of account, and new vs. existing account. This information should be made available to the public.

I would be glad to answer any questions about these suggestions.

Sincerely,

Malcolm Bush  
President