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Regulation Comments  
Chief Counsel's Office  
Office of Thrift Supervision  
1700 G Street NW  
Washington, DC 20552  
Attn: Number 2006-44

Re: **CRA Uniformity:** Proposed Changes to OTS Community Reinvestment Act Regulations; 71 Federal Register 67826; November 24, 2006

Ladies and Gentlemen:

The Office of Thrift Supervision (OTS) proposes to make changes to its current Community Reinvestment Act (CRA) regulations in four areas to establish interagency uniformity. These changes include: (1) changing the definition of "small savings associations" with \$251 million to \$1 billion in assets to "intermediate small savings associations" and establishing a new community development test for them; (2) eliminating the option for alternative weighting under the large retail savings association test; (3) indexing asset thresholds based on changes to the Consumer Price Index (CPI); and (4) clarifying the impact of discrimination on an association's CRA rating.

On behalf of the more than two million men and women who work in the nation's banks, the American Bankers Association (ABA) 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 holding companies, as well as savings associations, trust companies, savings banks, and bankers banks--makes ABA the largest banking trade association in the country.

### **Summary of Comments**

ABA believes the proposed alignment of OTS' CRA regulation with the rules of the other agencies is unwarranted. It was not OTS that deviated from the interagency standard of two baseline tests. It was not OTS that created the extra—and rather complicated—category of "intermediate small bank." Concerns expressed by community organizations that the streamlined test fails to recognize or encourage community development activity are unsupported by the record of experience or the interpretive guidance available for all agencies to apply. There is no reason to

impose three tests where two are effective in capturing both lending and community development performance. OTS' leadership in reducing undue burden should not be compromised by adding complications to its regulation where none is required. Community savings associations are committed to serving their neighborhoods; a new layer of regulation will do nothing to raise an already high level of commitment, but it will reduce the flexibility to provide those services most in need for each community.

ABA also believes that OTS should not change its current approach of permitting a savings association that is subject to the "large bank" test the flexibility to weight its lending, service, and investments in a way that best reflects its efforts to meet the credit needs of its community. This flexibility is appropriate and necessary given the differences in the thrift charter. ABA further believes indexing is a welcome concept, and should be applied to separate the boundary between a two test—not a three test—system. Finally, ABA supports having all similarly situated institutions' CRA ratings impacted by illegal discrimination or illegal credit practices in a similar manner.

## **Background**

The CRA regulatory reform of 1995 made two fundamental changes to the evaluation process. First, it recognized the need to evaluate performance over process. Second, it recognized that expectations about performance within the industry could best be divided between large institutions and small institutions. This division placed roughly 80% of industry assets in a category made subject to new reporting burdens and performance tests, while streamlining the performance criteria for small institutions.

Ten years later the banking agencies reviewed the CRA regulation. By then, industry and community organizations had finally learned how to apply the new regulation. After an extended public comment process, the four banking agencies jointly proposed three changes: an increase in the threshold separating small from large banks to \$500 million, incorporation of existing guidance on illegal credit practices into the regulation itself, and minor enhancements to data disclosures. No one proposed creating a third category of institutions with its own test that rebalances the elements of performance.

Only after OTS acted to set the dividing line between small and large institutions at a more appropriate level of \$1 billion—closer to the original division of industry asset coverage—did the other agencies re-invent the CRA evaluation process by creating a brand new category of banks and test criteria.

## **Discussion**

### 1. An intermediate bank category and test is unwarranted for small institutions.

The arguments being made for OTS alignment with the other banking agencies generally coalesce around the unsupported notion that the streamlined test that OTS applies, to what everyone concedes for reporting purposes are small institutions, either somehow weakens their CRA performance or impedes evaluating performance across industry segments. As demonstrated below, the small bank test as applied by OTS rebuts these criticisms and demonstrates that it achieves its original purpose of appropriately streamlining the CRA evaluation process without diminishing a

small bank's incentive for obtaining credit for community development activity. Consequently, an intermediate category and test applied to admittedly small banks is unwarranted.

*a. The streamlined test captures, encourages and enables comparison of community development activity.*

Interagency adoption of the streamlined test in 1995 acknowledged that most community banks fulfilled the statutory mandate of CRA to help meet the credit needs of their communities through their lending activity. This continues to be a fundamental truth even as the size of community banks has kept pace with economic growth and inflation. Nevertheless, from the beginning the streamlined test captured, encouraged and enabled comparison of small bank community development activity—whether through community development lending, qualified investments, or community development services.

**i. The streamlined test captures community development activity, as such activity has always been included as part of a small institution's exam criteria.** The 1995 CRA reform rule establishing the streamlined test explicitly includes community development lending and lending-related qualified investments as part of the performance criteria to be considered in preparing a bank or savings association's public evaluation. In addition, the Interagency CRA Q&As stress that even though regulatory performance criteria did not explicitly mention community development loans or lending-related qualified investments in the geographic distribution criteria they nonetheless can be considered for that factor. *Interagency CRA Q&As at .26 (a) Q/A 1.* Furthermore, the Q&As describing small institution performance ratings make clear that bank "performance in making qualified investments and providing services that enhance credit availability" count toward an outstanding rating, and that qualified investments, community development loans, and community development services can be considered even if they do not directly benefit the bank's assessment area. *Interagency CRA Q&As at .26(b) Q/A 1 and 2.*

**ii. The streamlined test encourages community development activity.** Some commenters on the OTS' rulemaking in 2004 criticized the OTS for significantly weakening the requirements of the Community Reinvestment Act on savings associations. Today, community group commenters are again mischaracterizing the impact of the streamlined test as applied by OTS. These comments are demonstrably misinformed, as is evident from the record of OTS examiner vigilance in evaluating savings associations' CRA performance. The OTS' regulation has not led to any diminution in savings associations' commitments to their communities. To illustrate this conclusion ABA staff reviewed 115 CRA Public Evaluations (PEs) of savings associations between \$250 million and \$1 billion in assets done since the OTS finalized its current CRA regulation. All of these examinations were done under the small savings association examination procedures, but all of these institutions would be placed into the more regulatory burdensome Intermediate Small Savings Association examination if the OTS adopts this proposal. At least three-quarters of these reviews

**Excerpt from a March 2005 PE for a small savings association (assets over \$400 million) rated Satisfactory.**

\_\_\_ FSB has been involved in a number of Community Development activities. ... granted a loan in the amount of \$1,000,000 to the \_\_\_\_\_ Municipal Development Authority. The loan was used to construct a new fire station .... This fire station is located in a moderate-income geography.

... is a participant in an \$18 million downtown renewal project known as \_\_\_\_\_ Square. ... participation is \$1 million. This project is located in a low-income geography.

... continues to participate in the \_\_\_\_\_ Housing Consortium Program, targeted to low- and moderate-income borrowers. This program utilizes federal funds to provide down payment monies to low-income first time homebuyers. Local financial institutions provide the first lien mortgage financing. The program includes relaxed underwriting requirements and completion of an extensive homeownership education program. ... funded four loans totaling \$182,250.

recognize significant community development lending, qualified investments or community development services provided by the particular savings association being examined. Many of these evaluations result in “outstanding” ratings, while others illustrate performance by savings associations that are rated “satisfactory.” (See Sidebars for actual examples from OTS PEs.)

Sampling from these evaluations discloses that savings associations engage in the following types of community development activities—many of which some commenters wrongly suggest savings associations will not do, or get credit for, under the streamlined test, even though they are doing them now and have been doing them for years:

- \$38,400 loan to Habitat for Humanity
- \$750,000 loan to a Christian Fellowship that provides assistance to LMI families
- \$132,000 loan to program for re-integrating juveniles to the community after incarceration
- Providing 170 hours of financial education to seniors
- Providing 750 hours of marketing assistance to various community groups to help them reach their LMI constituents
- Purchasing a \$500,000 tax credit for a housing project for low-income migrant workers
- Making 67 qualified investments in the form of grants to various local organizations
- Sponsoring successful Affordable Housing Award applications
- Participating in municipal projects that provide renewal to low- or moderate-income geographies

This is of necessity only a partial list. A savings association’s PE regularly contains statements, paragraphs and sometimes full pages of narrative explanation detailing the savings association’s particular community development activities. There is simply no doubt that savings associations under \$1 billion in asset size have sufficient encouragement and receive explicit credit for a full range of both common and innovative community development activities.

**iii. The streamlined test enables comparison of community development activity.**

The extensive narratives prepared by OTS examiners make the CRA record of a savings association readily comparable to the record of any bank—for anyone who takes the time to examine the PEs. ABA urges everyone to compare OTS narratives with the evaluations prepared by the other agencies of similarly sized banks. The ability to compare banks and savings associations with their different charter authorities is not improved by reducing actual performance to a simple

**Excerpt from a November 2005 PE for a small savings association (assets over \$300 million) rated Outstanding.**

... Federal has taken the lead in supporting community development in its community by providing community development lending, financial services, and qualified investments.... The institution recently became a member of Community Lender’s Community Development Corporation (CLCDC), an organization that provides financing and investing in community development projects.

Management purchased land and is constructing its administrative office and loan center in a moderate-income geography, which is helping to contribute to the revitalization of \_\_\_\_\_. This complex should be ready for occupancy late 2005, and provide employment opportunities in the area.

Loans were funded to non-profit organizations that provide various community development services to the local community. Participation funding was also provided for a low-income and elderly housing project of modular units.

The institution offers a first-time homebuyer program. During the review period 21 loans totaling \$2.4 million were made. This program offers favorable features that provide the opportunity for a low- and moderate-income borrower to purchase their first home.

... Federal made charitable contributions to several organizations that provide community development services to those in need. Nine thousand was donated to a camp for mentally challenged youth and \$3 thousand to a health facility providing free health care to disadvantaged persons.

As part of its commitment to the community, ... Federal donates 10 percent of after tax profits to public service organizations, charities, community events and downtown revitalization. A total of \$168 thousand was donated, of which approximately 21 percent of those philanthropic activities qualify for Community Reinvestment Act consideration.

rating. The real value of the PE is that information is provided in the narrative that enables interested parties to understand each institution's performance context, the opportunities available and the responsiveness of particular activities to the local communities' needs. Anyone, by reading the PE, delving behind the overall ratings and considering the qualifications of different activities that earn recognition, can make meaningful comparisons between institutions. ABA finds that the OTS' application of the streamlined test enables interested readers to do this perfectly well, and we believe that adding a whole new CRA examination for intermediate small savings associations will not improve the ability to compare the CRA performance of these institutions. In fact, the current program encourages flexibility and innovation, rather than routine cookie cutter approaches, without limiting the ability to evaluate achievement in a genuine qualitative and quantitative way. We fear that the proposed regulatory change will sacrifice much innovation, flexibility, and qualitative evaluation, for the sake of mere "uniformity."

*b. Small banks are small banks and need not be assigned two different categories.*

Since the 1995 reform effort the depository institution industry has continued to evolve and consolidate. Based on September 30, 2006, FDIC data, institutions over \$1 billion in assets account for 87.4% of industry assets. This means that proportionately and in absolute dollars more banking assets are covered under the \$1 billion large institution test today than were covered in 1995 when the small bank/large bank distinction was first established and set at \$250 million.

One thing remains true. As in 1995, community banks survive when they have strong lending programs that are responsive to the needs of their communities. Today those banks may be nominally larger in asset size, but all the reasons for providing them with a streamlined test remain valid. Any distinction between a \$200 million, \$400 million or \$950 million dollar bank has nothing to do with the basis on which their CRA performance should be evaluated. The boundary between small and intermediate small only creates more interpretive issues and more examination work, not better CRA performance. It is the essence of unnecessary burden.

If having identical CRA rules is truly an interagency goal, then it is the other agencies that should align with OTS and return to evaluating all small banks under the original streamlined test.

In summary, as OTS underscores in its notice for comment, "OTS believes savings associations will continue to serve their markets, including low- and moderate-income communities, regardless of the applicable CRA rules." ABA agrees with this fully. It is true for community savings associations as well as community banks. ABA further believes that this reality proves that there is no need for three bank categories and a third test when two tests will do—and have done—perfectly fine in evaluating and enabling comparison of CRA performance.

## 2. Keep flexible large test component weights to recognize charter and business plan differences.

When the Community Reinvestment Act was enacted in 1977, the savings association charter was very different from the commercial bank charter. Savings associations were primarily to be home mortgage lenders, and their investment and lending powers were significantly limited compared to commercial banks. In 1995, when the Agencies revised the CRA regulations to include a large institution test subject to separate lending, service and investment tests, the Agencies recognized those differences in lending and investment powers in their discussion of the final CRA regulation.

The supplementary information contained in the 1995 reform rule stated as follows:

Several thrift commenters had concerns about the application of the investment test to thrift institutions because of their limited investment authority. Rather than providing a blanket exemption from the investment test, the final rule modifies the ‘capacity and constraints’ section of the performance context to clarify that examiners should consider an institution’s investment authority in evaluating performance under the investment test. A thrift that has few or no qualified investments may still be considered to be performing adequately under the investment test if, for example, the institution is particularly effective in responding to the community’s credit needs through community development lending activities....<sup>1</sup>

Again from the supplementary information in the 1995 rule:

As previously discussed, the final rule has modified the performance context for CRA evaluations to account for financial institutions with limited investment authority. These modifications would permit an institution with limited authority to make investments to receive a low satisfactory rating under the investment test, although it has made few or no qualified investments, if the institution has a strong lending record, thereby preventing potential anomalies in the CRA performance ratings.<sup>2</sup>

Or to put it another way, even though it looks like the Agencies adopted a uniform rule in 1995, they did not in actual practice because it made no sense to do so, given the differences in charter powers.

OTS’ implementation of an option for large institutions to adjust the weight of the components of the large bank test recognizes more explicitly that thrifts have always had a *de facto* different weighting for the level of performance to be expected of them under the investment test. This no more undermines inter-bank comparability than such comparability was undermined under the large test without explicit weighting flexibility. In fact, it can be argued that by making the weighting explicit, comparability is enhanced. Thrifts whose investment options are limited will now more likely make clear how their performance will be rebalanced to make up for that limit than was apparent from applying the more obscure performance context rule recited in the details of the rule preamble. Once again, all one has to do is read to compare.

In addition, ABA notes that the 1995 CRA reform afforded banks the opportunity to rebalance their CRA performance under the strategic plan option. This enabled banks with different business plans to re-craft the criteria against which they would be evaluated. The agencies anticipated that non-traditional business plans would not fit the one-size-fits-all large bank test and sought to add flexibility. By permitting a simpler means of weighting large bank test components, OTS cut through the compliance hurdles that had discouraged use of the strategic plan option between 1995 and 2004 and made the notion of matching unique business plans with tailored CRA criteria a more accessible alternative. We would once again emphasize that innovation and experimentation are often the keys to successful community development, all of which is encouraged by the existing process that the proposed rule would sacrifice.

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<sup>1</sup> 86 FR 22163 (May 4, 1995).

<sup>2</sup> Id at 22166.

In summary, ABA urges OTS to maintain its flexible weighting option for large savings association test components as a worthy advance that improves CRA performance evaluation and enhances comparability across large institutions of differing charter authority and business models. Alignment by OTS with the other banking agencies would only make CRA evaluations more rigid and less responsive to community needs and banking operation realities—just another name for burdensome and reduced performance.

3. Adopt threshold indexing and conform illegal credit practices rating standards.

OTS proposes to make two changes to make OTS rules uniform with the Agencies: (1) to index the asset size of small institutions in the same way and to the same index as the other Agencies and (2) to treat evidence of illegal discrimination or other illegal credit practices as sufficient grounds to reduce an institution’s ratings. ABA supported both of these regulatory provisions in the other Agencies’ rulemaking, and ABA supports the OTS in making these changes.

**Conclusion**

The ABA believes that OTS should not change the definition of a small savings association. This change would impose upon associations the additional “intermediate small institution” test and result in little, if any, benefit. The ABA further believes that elimination of the alternative weighting option for lending, investment and service under the large, retail savings association test is not advisable. Further, ABA believes that the OTS has good legal and practical grounds for its current CRA regulations, given the uniquely different charter for savings associations. Thus, the ABA urges the OTS not to adopt these parts of the proposal. However, the ABA supports annually indexing the asset threshold. We also support the proposal to consider evidence of discrimination or other illegal credit practices in associations’ CRA evaluations. If there are any questions regarding these comments, please do not hesitate to contact either of the undersigned.

Sincerely,



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