CONSUMER MORTGAGE COALITION

April 6, 2004

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The Honorable Jennifer J. Johnson
Secretary
Board of Governors of the Federal Reserve System
20th Street and Constitution Avenue, NW
Washington, DC 20551
Docket No. R-1181

Communications Division
Public Information Room, Mailstop 1-5
Office of the Comptroller of the Currency
250 E Street, SW
Washington, DC 20219
Docket No. 04-06

Mr. Robert E. Feldman
Executive Secretary
Federal Deposit Insurance Corporation
550 17th Street, NW
Washington, DC 20429
Attention: Comments

Regulation Comments
Chief Counsel's Office
Office of Thrift Supervision
1700 G Street, NW
Washington, DC 20552
Attention: No. 2004-04

Re: Community Reinvestment Act Regulations—Joint Proposed Rulemaking, 69 Fed. Reg. 5729 (February 6, 2004)

The Consumer Mortgage Coalition ("CMC"), a trade group of national mortgage lenders, servicers, and service providers appreciates the opportunity to submit its views concerning the joint proposal (the "Proposal") of the federal bank regulatory agencies (the "Agencies") to make changes to the Community Reinvestment Act ("CRA") regulations. 69 Fed. Reg. 5729 (February 6, 2004).

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The CMC's members support the policies and goals of meeting the credit needs of all segments of communities, including low- and moderate-income neighborhoods, set forth in CRA. We commend the Agencies' efforts to support the policies and goals of the CRA by amending the CRA regulations. We are concerned, however, that the Proposal will not only detract from the CRA's purpose, but also reduce an institution's ability to meet the credit needs of its community.

This letter focuses on the Proposal's revisions to section ___.28(c) of the regulations, which would allow the Agencies to consider violations of other laws when assigning a CRA rating. We believe that these changes, although well-intentioned, would have a negative impact on consumers and lenders' abilities to meet the credit needs of its diverse consumers, and, therefore, urge the Agencies to not adopt them.

Consideration of Violations of Other Laws and Abusive Lending Practices

The Agencies propose to "address abusive lending practices in CRA evaluations" by allowing the Agencies to take into account "evidence that the institution, or any affiliate the loans of which have been included in the institution's performance evaluation, has engaged in illegal credit practices, including unfair or deceptive practices." 69 Fed. Reg. 5729, 5730.

The current regulations state that "[e]vidence of discriminatory or other illegal credit practices adversely affects the [agency's] evaluation of [an institution's] performance. In determining the effect on the [institution's] assigned rating, the [agency] considers the nature and extent of the evidence, the policies and procedures that the [institution] has in place to prevent discriminatory or other illegal credit practices, any corrective action that the [institution] has taken or has committed to take, particularly voluntary corrective action resulting from self-assessment, and other relevant information." Interagency CRA Regulations, 12 C.F.R. § ___.28(c). The Agencies propose to expand the current requirement in several ways:

- The regulation would include a list of violations of specific statutory provisions that would have an adverse impact on an institution's CRA evaluation.

- The regulation would state that engaging in a legal practice that is perceived by the Agency to be "abusive" would be viewed negatively.

- The proposed list of violations includes unfair or deceptive acts or practices ("UDAPs") under the Federal Trade Commission ("FTC") Act, which are not prohibited under substantive federal banking regulations. [Do the members wish to challenge the banking agencies from incorporating FTCA violations in the CRA assessment?]

- The regulation would provide that evidence of discriminatory, other illegal, and abusive credit practices of an affiliate will be considered if any loans of that affiliate were considered in the CRA evaluation for an assessment area.

Although the Proposal is well intended, it will detract from the focused purpose of the CRA and its current regulations, and could have the perverse effect of reducing the ability of an institution to "meet . . . the credit needs of its entire community, including low- and moderate-income neighborhoods"—the goal of the CRA.

The CRA's Purpose

The overarching purpose of the CRA is to encourage financial institutions to help meet the credit needs of consumers:

> It is the purpose of this title to require each appropriate Federal financial supervisory agency to use its authority when examining financial institutions, to encourage such institutions to *help meet the credit needs of the local communities* in which they are chartered consistent with the safe and sound operation of such institutions.

12 U.S.C. § 2901(b) (emphasis added). The regulations promulgated under the CRA should be focused on promoting the goal of the CRA alone. The Proposal, however, would have the effect of requiring the Agencies to monitor the compliance of a financial institution, as well as all affiliates lending in any assessment area for which the institution provides data on any affiliate, with the Equal Credit Opportunity Act, the Fair Housing Act, the Home Ownership and Equity Protection Act, the Federal Trade Commission Act, the Real Estate Settlement and Procedures Act, and the Truth in Lending Act, as well as other applicable Federal and state laws. Further, the Proposal requires that a financial institution's evaluation be "adversely affected by discriminatory, other illegal, or *abusive* credit practices." 69 Fed. Reg. 5740 (emphasis added).

While the CMC and its members support compliance with each of these laws, Congress enacted each law for a specific purpose and each law has its own regulations to ensure compliance. The Agencies, in conjunction with other federal agencies, already have the authority to monitor compliance with such laws, and regularly and rigorously examine institutions for their compliance with them. We are not aware of any authority in the CRA that permits or encourages the Agencies to consider compliance with the myriad separate state and federal laws that govern consumer lending when evaluating a financial institution's compliance with the CRA. Rather, the statute seeks a balance between ensuring the safe and sound operation of an institution and ensuring that the institution is providing credit throughout the communities it serves. Thus, any effort to address compliance issues in the context of the CRA evaluation should be focused on ways that the non-compliance had a materially negative effect on the institution's efforts to meet the credit needs of the communities it serves.

Still, we are mindful of the logic underlying the Proposal—the concern that an institution should not receive positive treatment for loans that violate certain crucial consumer protection provisions. We suggest that the current regulation quoted above already provides the agencies with a suitable mechanism to address this concern. If evidence exists that the institution is engaged in systematic or widespread non-compliance, particularly in the area of lending discrimination, the examiners appropriately take that

fact into their assessment of the institution, including in their assessment the steps the institution has taken to correct issues it has created and prevents further non-compliance in the future. This mechanism is generally in line with bank examination process and structure.

Nonetheless, if the Agencies determine that a change of some sort is necessary, it is crucial that the Agencies look for and consider only systematic patterns of abuse and deception rather than entering the bottomless pit of reviewing individual instances of noncompliance. We can see how systematic equity-based lending focused in one neighborhood could have material negative consequences if numerous foreclosures result. Still, we strongly disagree that a variety of individual instances of non-compliance that cannot be shown to have truly affected the way any institution has met the credit needs of any community are appropriate to be considered for purposes of the CRA. If the Agencies end up reviewing non-systematic conduct, they will inappropriately refocus CRA examination away from meeting the needs of the community into an assessment of legal compliance by the institution and its affiliates.

The enumeration in the regulation of specific illegal conduct, and even of conduct that is not illegal but that an examiner might view as "abusive," would be contrary to the spirit of CRA. CRA review is not intended to be a part of law enforcement, but is designed to ensure that, "[i]n connection with its examination of a financial institution," the regulator considers, not only whether the institution is operating in a safe and sound manner, but also whether, in conducting its affairs, it is "meeting the credit needs of its entire community, including low- and moderate-income neighborhoods." 12 U.S.C. § 2903(a), (a)(1). The CRA is designed to correct a perceived defect in the regulatory structure, in which an examination that only considered safety and soundness might create incentives for institutions to avoid making loans and investments to the parts of the community that are most in need of the institution's services.

Recognizing the purpose of the CRA, the Agencies wisely decided not to structure the performance tests in 12 C.F.R. § ___.21 as an adversary proceeding, designed to discover evidence of violations, but as an informal information-gathering process. The Proposal could transform what should be a constructive process into an adjunct of the compliance examination, particularly if the Agencies adopt the proposal to give an adverse weight to practices that are legal but are perceived as abusive.

The current regulatory provision allowing consideration of illegal discrimination and other illegal practices itself represents an aggressive view of the agencies' authority under the CRA to evaluate whether the institution is "meeting the credit needs of its entire community," 12 U.S.C. § 2903(a)(1), but may be justified if it is read narrowly, as allowing an agency to consider evidence of practices that have a materially negative impact on whether the institution is meeting the community's credit needs. The CMC agrees that an institution that illegally discriminates against a segment of its community in its credit underwriting cannot be said to be meeting the community's credit needs. Similarly, if a loan is obtained through fraud, misrepresentation, or other illegal means, it should not be counted for CRA purposes. Of course, the current rule would easily capture these examples.

The Proposal, however, goes far beyond the statement in the current regulation to identify "violations" that trigger a negative CRA evaluation. The list appears to include practices that the Agencies regard as likely to have a negative impact on meeting credit needs, but many of the provisions listed are highly technical and a violation should not necessarily be regarded as bearing on whether an institution is meeting the credit needs of the community. For example, should an institution that made a calculation error that resulted in some consumers not receiving required HOEPA disclosures, with no evidence of any consumer injury resulting from the violation, be penalized under CRA, in addition to whatever administrative penalties or civil liability that the institution may also incur? The Proposal appears to attempt to address this issue in the statement in proposed section __.28(c)(2) that the agency "considers the nature" of the practices as well as any corrective action that the institution has taken, but the regulation should also expressly state that a practice that does not have a materially negative impact on whether the institution meets community credit needs is not considered in the CRA evaluation. Including a materiality standard would also avoid subjecting an institution to "double jeopardy" for a law violation for which it has already been penalized, and would allow institutions to enter into settlements of the underlying charges without fearing additional costs arising from a bad CRA rating.

Moreover, monitoring an affiliate's compliance with such laws removes the Proposal even further from the focus of the CRA. The CRA was enacted, in part, to discourage a bank from siphoning capital, in the form of deposits, from underserved parts of the community in which the bank operates and then investing the deposits in loans made to already well-served parts of the bank's community. Under the CRA, a depository institution is asked to "reinvest" a share of its deposits and to return the benefit of having FDIC insurance by extending credit to the consumers within its community. The Proposal's inclusion of affiliates in the CRA examination, which, as discussed above, would include an evaluation of all practices under a panoply of statutes, would turn the compliance process into a global consumer compliance investigation. The Agencies do not have the resources to complete such an investigation fairly among all financial institutions and would create the overwhelming process of examining non-bank affiliates. Focusing the Agencies' limited resources on such expansive investigations would undermine the CRA's focused purpose of extending credit to all segments of the community.

"Abusive" Lending Practices

The CMC's members strive to maintain the highest standards when providing credit to customers. We are concerned, however, with the Proposal's expansion of the CRA regulations to require an adverse CRA rating if an institution engages in "abusive" credit practices. While the change to section ____.28(c) only specifically addresses "a pattern or practice of lending based predominantly on the foreclosure or liquidation value of the collateral," the Agencies discuss in the commentary that they will "consider all credible evidence of discriminatory, other illegal or abusive credit practices." 69 Fed. Reg. at 5743-44, 5741.

The CMC's members strongly condemn abusive lending practices and endeavor to meet the needs of its consumers with safe and sound lending practices. Yet the Proposal's attempt to infuse the CRA and financial institution evaluations with the still undefined area of "abusive" lending will lead to unnecessary confusion. Financial institutions and affiliates already have to ascertain the scope of the various state and local predatory statutes and comply with the conflicting mandates of each such statute. A comprehensive and uniform standard defining "abusive" or "predatory" lending has not been developed. Lack of a clear standard and increasingly vague definitions of "abusive" practices in state statutes and local ordinances have at times resulted in lenders refusing to originate loans in certain jurisdictions for fear of violating such broad statutory guidelines, thus making fewer credit products available to their consumers—a result that is in direct opposition to the purpose of the CRA.

There is no justification for penalizing institutions under CRA for practices that the Agencies view as "abusive" or "predatory" but which are not illegal. If a practice is genuinely abusive, it should be prohibited by federal or state law or regulation; if it is not, then an institution should not be penalized for engaging in it. For example, some may believe (and some jurisdictions have concluded) that the HOEPA triggers should be set at a lower level than provided in Regulation Z. Is it *per se* "abusive" to make a nonprime loan that is near but below the HOEPA triggers and include a contractual clause that would be prohibited if the loan were subject to HOEPA? Others believe that it is "abusive" for a lender to pay a "yield spread premium" to a mortgage broker, rather than a fixed fee for services rendered, but the courts have repeatedly upheld the general legality of such fees under the Real Estate Settlement Procedures Act. Some may believe that these practices are abusive in a colloquial sense, but Congress and the Federal Reserve Board have set a cutoff below which such a practice, without more, is not legally "abusive." Using a standard that is not tied to actual legal restrictions will invite subjectivity and will be very difficult in practice to administer similarly across the country.

When the Agencies consider "all credible evidence of discriminatory, other illegal or abusive credit practices," which standard will financial institutions and affiliates be measured against? Aside from the Agencies contacting all 50 state regulators to discuss each state's predatory lending provisions in relation to an institution's evaluation, neither the financial institutions, nor the Agencies are equipped with a clear, standard definition of "abusive" or "predatory" lending. Attempting to discuss a financial institution's and its affiliates' lending practices with as many as 50 state regulators will undoubtedly expand the regulatory burden of the CRA, as well as strain the resources of the Agencies.

Additionally, while the Agencies state that taking a financial institution's and affiliate's practice of discriminatory, other illegal or abusive credit practices into account for purposes of a CRA rating will not involve "specific evaluation of individual complaints or specific evaluation of individual loans," such a statement will not limit the burden an institution will face in cooperating with the Agencies during such an examination. If individual instances of purported misconduct are reported to the examiners, for example by a community or advocacy group, it is likely that the examiners will ask the institution to comment on the submitted instances. An institution that did not respond to the comments would be considered guilty of "abuse" until proven innocent. If the examiners

did not request comment from the institution, particularly regarding the conduct of an affiliate that is not federally examined, then the use of the information would be even more unfair. With major affiliates that are not subject to compliance examination by the Agencies, it would be very difficult for examiners to determine whether, for example, a dozen submitted instances showed a clear pattern of misconduct or were the usual hodge-podge of random errors. Only an examination—which the examiners do not have the authority to conduct—would do so fairly. As a result, we expect that in practice, the Proposal, if adopted, would at the very least lead to the evaluation and discussion of a multitude of individual complaints. More likely, it would lead to some sort of quasi-examination of affiliate lending practices. This would be a completely unwarranted expansion of CRA, supported neither by the statute nor the underlying public policy.

One other foreseeable result of this process is that the Proposal will likely result in greatly adding to the existing and increasingly burdensome record-keeping and reporting requirements under CRA.

Incorporation of the FTC Act

The prohibition against UDAPs in Section 5 of the FTC Act is very broad, and including it on the list invites community activists to raise UDAP complaints against virtually every institution. The Agencies should either remove it from the list or, at a minimum, narrow it to unfair or deceptive credit practices that have a materially negative impact on the institution's ability to meet community credit needs.

Practices of Affiliates

The Agencies propose to state specifically that discriminatory, other illegal, or "abusive" practices of an affiliate may adversely impact the CRA evaluation within an assessment area if the institution has chosen to have the affiliates' activities considered in the evaluation of the assessment area. The Agencies also seek comment on whether these practices should be considered even if they did not occur within an assessment area. As noted above, we believe that only illegal practices should be considered, and that they should be considered only to the extent that they had a material impact on the institution's ability to meet the credit needs of a particular community that the financial institution serves. Illegal practices of an affiliate should be subject to the same standard, and, accordingly, practices that occurred outside of an assessment area should have no bearing (either positively or negatively) on an institution's CRA rating.

Further, if Agencies are required to consider an affiliate's lending activities, whether or not the activities are inside any of the financial institution's assessment areas, the Proposal could have the effect of a financial institution losing the non-banking powers granted by the Gramm-Leach-Bliley Act (the "GLB Act"). By taking all of an affiliate's lending activities into account for purposes of a financial institution's CRA rating, regardless of whether such lending activities had a material impact on the institution's ability to serve the credit needs of its community, the Proposal substantially increases the risk that not all of a financial holding company's depository institutions will receive a satisfactory or better CRA rating. While we agree with the Agencies' rejection of a *per se* standard that automatically mandates a below satisfactory rating for any abusive

lending practice, the possibility of an institution receiving a below satisfactory rating because of an affiliate's lending in *all* areas is significant, thus resulting in dramatic GLB consequences—preventing a financial institution from engaging in non-banking activities. If Congress had intended for the Agencies to consider all of a financial institution's lending activities in their CRA examination for purposes of determining whether an institution may engage in securities and insurance activities, Congress would have included such language in the GLB Act. At present, no such authority exists, and if enacted, the Proposal would greatly undermine the purpose of the GLB Act—to allow financial holding companies to engage in a broad array of financially related activities.

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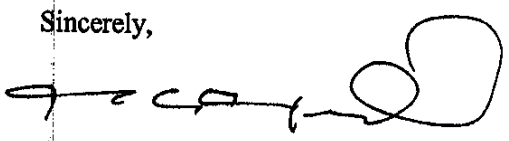
Once again, the CMC appreciates the opportunity to comment on the Agencies' Proposal. While we support the Agencies' ongoing efforts to improve the regulations issued under CRA, for the reasons stated, we urge the Agencies not to adopt the changes to section ____.28(c) that would allow the Agencies to consider violations of other laws, as well as abusive lending practices of financial institutions and their affiliates, when assigning a CRA rating.

Sincerely,



Anne C. Canfield
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