NATIONAL COMMUNITY REINVESTMENT COALITION

NCRC

27

web

*John E. Taylor*
President & CEO

**Board of Directors**
*Pete Garcia, Chairperson* Chicanos Por La Causa, Inc.
*Ted Wysocki, Vice Chairperson* Chicago Association of Neighborhood Development Organizations (CANDO)
*Hubert Van Tol, Vice Chairperson* Fairness in Rural Lending
*Shelley Sheehy, Secretary* Rural Housing Institute, Inc.
*Elbert Jones, Treasurer* Community Equity Investments, Inc.
*Gail Burks, Past Chairperson* Nevada Fair Housing Center, Inc.
*Marva Smith Battle-Bey* Vermont Slauson Economic Development Corporation
*Lee Beaulac* Rural Opportunities, Inc.
*Malcolm Bush* Woodstock Institute
*Stephan Fairfield* Fifth Ward Community Redevelopment Corporation
*Alan Fisher* California Reinvestment Committee
*Devorah Lee Fong* Spring Creek Community Corporation
*Edward J. Gorman, III* American Community Partnerships
*Irvin Henderson* Community Reinvestment Association of North Carolina
*Alan Jennings* Community Action Committee of Lehigh Valley
*Matthew Lee* Inner City Press/ Community on the Move
*Maryellen Lewis* MSU Community & Economic Development
*Dean Lovelace* Dayton Community Reinvestment Institute
*Eugene Lowe* U.S. Conference of Mayors
*Moises Loza* Housing Assistance Council
*Ernest E. (Gene) Ortega* Home Education Livelihood Program
*Rashmi Rangan* Delaware Community Reinvestment Action Council
*Cameron Whitman* Center for Policy & Federal Relations
*Morris Williams* Coalition of Neighborhoods
*Veronica Williams* Detroit Alliance for Fair Banking
*F. Barton Harvey, III* Chairperson Emeritus The Enterprise Foundation

733 15th Street, NW Suite 540
Washington, DC 20005-2129
Phone: 202 628-8866
Fax: 202 628-9800
Website: www.ncrc.org

October 2, 2001

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

Docket No. 01-16
Communications Division
Public Information Room
Mailstop 1-5
Office of the Comptroller of the Currency
250 E St. SW
Washington DC 20219

Robert E. Feldman
Executive Secretary
Attention: Comments/OES
Federal Deposit Insurance Corporation
550 17th St. NW
Washington DC 20429

Regulation Comments
Chief Counsel's Office
Office of Thrift Supervision
1700 G St. NW
Washington DC 20552
Attention: Docket No. 2001-49

Dear Officials of Federal Banking Agencies:

The Community Reinvestment Act (CRA) has been instrumental in increasing lending and investing to low- and moderate-income communities across the country. The regulatory changes to CRA during 1995 strengthened CRA exams by emphasizing a bank's performance in providing services and in making loans and investments. The federal banking agencies must now update the CRA regulations in order to further reinvestment in low- and moderate-income communities, as well as in underserved minority communities.

The results of the positive changes to the CRA regulation in 1995 have been significant. The Department of Treasury's study on CRA found that lending to low- and moderate-income neighborhoods is higher in geographical areas that banks designate as their CRA assessment areas than in areas where banks are not examined under CRA.

By reducing discrimination and barriers to information, CRA has improved the efficiency of the marketplace and has increased lending. Partnerships between lending institutions and community groups discover new methods of loan underwriting and marketing that are more effective in reaching underserved communities. NCRC's 800 member organizations have established such partnerships that have created additional profitable business opportunities for banks (please see the appendix, which includes a NCRC report about profitable lending programs involving our member organizations). Some of these innovative partnerships would have occurred in the absence of CRA, but not close to the same breadth and depth.

To preserve the progress in community reinvestment, the federal banking agencies must update CRA to take into account the revolutionary changes in the financial industry. The Gramm-Leach-Bliley Act of 1999 allowed mergers among banks, insurance companies, and securities firms. Banks and thrifts with insurance company affiliates are now aggressively training insurance brokers to make loans. Securities affiliates of banks offer mutual funds with checking accounts. Mortgage company affiliates of banks continue to make a significant portion of the total loans, often issuing more than half of a bank's loans. The CRA regulation now allows banks to choose whether the lending, investing, or service activities of their affiliates will be considered on CRA exams. NCRC strongly urges the regulatory agencies to mandate that all lending and banking activities of non-depository affiliates must be included on CRA exams.

The CRA procedures for delineating assessment areas also need to be changed if CRA is to adequately capture the activities of banks in the rapidly evolving financial marketplace. Presently, CRA exams scrutinize a bank's performance in geographical areas where a bank has branches and deposit-taking ATMs. Banks are increasingly using brokers and other non-branch platforms to make loans. As a result, CRA exams of large, non-traditional banks scrutinize a tiny fraction of bank lending. This directly contradicts the CRA statute's purpose of ensuring that credit needs in all the communities in which a bank is chartered are met.[1] NCRC believes that the CRA regulations must specify that a bank's CRA exam will include communities in which a great majority of a bank's loans are made.

If CRA exams hope to keep pace with the changes in lending activity, NCRC strongly believes that CRA exams must rigorously and carefully evaluate subprime lending. As explained in more detail below, NCRC maintains that subprime lending must not count as much as prime lending on CRA exams and that CRA exams must severely penalize any subprime lending that is predatory.

The CRA regulations must also be changed to explicitly consider minorities on the lending test just like low- and moderate-income borrowers and communities. Considerable research has revealed the

[1] 12 USC 2901, Title VII of Pub. L. 95-128, 91 Stat. 1147 (October 12, 1977).

domination of subprime lenders in refinance and home equity lending in minority communities. This lopsided market confronts minorities with few alternatives to high cost refinance lending. If minorities were an explicit part of the lending test, CRA exams would stimulate more prime lending in communities of color.

Segments of the banking industry will seek to weaken the CRA regulations and examinations. They will ask for the elimination of the investment test on large bank exams. They will also urge that more banks be allowed to qualify for the streamlined small bank exam and for the streamlined wholesale and limited purpose exam. NCRC vigorously opposes the elimination of the investment test since low- and moderate-income communities experience a shortage of equity investments for small businesses and other pressing economic development needs. The present CRA exams are reasonable and are not burdensome for banks. Allowing more banks to qualify for streamlined exams will simply weaken CRA enforcement.

While CRA has played a significant role in increasing access to credit, much more progress is needed. Redlining and reverse redlining (predatory lending) still plague minority and working class communities. Market failure and barriers to information remain that prevent creditworthy and hardworking residents of underserved communities from receiving the prime loans that they need to purchase homes, start small businesses, and provide for their families. The flip side of discrimination is that lenders are still missing out on profitable lending opportunities. CRA needs to be updated to keep pace with the changes in the marketplace. Any diminution of CRA will ultimately weaken the nation's economy since market imperfections would once again become more pronounced in minority and working class communities.

NCRC's detailed comments in response to the questions posed by the Advance Notice for Proposed Rulemaking (ANPR) are the following:

**Update Assessment Area Procedures**

The practice of narrowly defining assessment areas to include only geographical areas containing a bank's branches and its main office often misses the great majority of a non-traditional bank's loans and purchases of loans. This is the case with CRA exams of subprime lenders, including Provident Bank, regulated by the Federal Reserve Board and Superior Bank, FSB, regulated by the Office of Thrift Supervision. The recently closed Superior had an absurd assessment area that covered only 1.3 percent of the institution's loans.[2] In other words, the CRA exam did not investigate more than 98 percent of the institution's loans and purchases of loans. Provident's assessment area comprised 41 percent of its loans; about 60 percent of the bank's lending activity was not considered on the CRA exam.[3]

[2] CRA Performance Evaluation of Superior Bank, FSB, Docket # 08566, Office of Thrift Supervision Central Region, September 27, 1999.
[3] CRA Performance Evaluation of Provident Bank, Docket # 612618, Federal Reserve Bank of Cleveland, July 12, 1999.

Likewise, State Farm's new thrift has an assessment area that covers only 21 percent of its lending activity although a March 2000 exam states that State Farm intends to use its Internet site and its insurance agents to make loans across the country.[4]

An analysis of the top lenders in the Phoenix metropolitan area likewise illustrates the inadequacy of the current assessment area procedures. In 1999, Chase Manhattan Mortgage, National City Mortgage, and Washington Mutual were among the top 10 largest lenders in terms of the number of single family loans made in the Phoenix area according to CRA Wiz™. Combined, they made 10,153 loans and had a market share of 6.4 percent. After excluding independent mortgage companies exempt from CRA, these three lenders were the fourth, fifth, and sixth largest lenders. Yet, the CRA exams of these three lenders and their affiliates did not include the Phoenix metropolitan area as an assessment area. Without regular CRA exams, the general public does not have much assurance that these large lenders in their community will meet its credit needs.

Often the largest financial institutions have assessment areas that skip from one metropolitan area to the next without acknowledging the rural areas in between. With the current efforts by many large financial institutions to expand their subprime lending, this issue has taken on critical importance. A company that has been predominantly a creature of major metropolitan areas can purchase a subprime lender that has an extensive rural network and never acknowledge those rural communities as part of its assessment area. As a result the residents of those rural communities, including Indian reservations, are swamped with subprime solicitations from major financial institutions, but do not have the benefit of competition on the prime product level. Requiring financial institutions to include counties and communities in which their non-bank affiliates do significant business as assessment areas would help protect rural areas from a lack of choice between prime and subprime products.

Harvard University recently concluded that banks make a higher percentage of their prime loans to LMI (low- and moderate-income) communities in their assessment areas than to those not in their assessment areas.[5] When only a few of the bank's service areas are included on CRA exams, a bank's lending to low- and moderate-income communities is reduced significantly. The current practice of defining assessment areas is a mockery of the CRA statute's stated purpose of ensuring that an institution serves the credit needs of all the communities in which they are chartered consistent with safety and soundness.

NCRC believes a straightforward definition of assessment areas for the new banking era is geographical areas where a depository institution and/or its affiliates have branches, offices, ATMs, and/or areas where they have more than one half of a percent of the market in loans. One half of a percent of the market often translates into hundreds of loans. NCRC's proposed definition of assessment areas would

---

[4] CRA Performance Evaluation of State Farm Financial Services, FSB, Docket # 14640, Office of Thrift Supervision Central Region, March 20, 2000.

[5] Joint Center for Housing Studies of Harvard University, *The Effect of the Community Reinvestment Act on Bank and Thrift Home Purchase Mortgage Lending*, August 2001. This paper updates the work that the Joint Housing Center had done for the Treasury Department reports on CRA as required by the Gramm-Leach-Bliley Act. The report includes a chart showing that CRA covered lenders and their affiliates are much more likely than non-CRA lenders to make prime loans to LMI borrowers and areas.

ensure that lending institutions are examined in all areas in which they are chartered and in which they engage in a significant amount of their business. At the very least, the federal banking agencies can stipulate in the CRA regulation that assessment areas will be those areas containing a great majority of an institution's loans.

The federal banking agencies implicitly recognize the unacceptability of assessment areas covering small percentages of loans. The CRA regulations state, for example, that a bank is likely to earn a needs-to-improve rating if a "small percentage of its loans" are made in its assessment area(s) and a substantial noncompliance rating if a "very small percentage of loans are made in the assessment area(s)."[6] CRA exams, including the one of Superior Bank, have already penalized banks and thrifts for very small percentages of loans inside their assessment areas. NCRC maintains, however, that the penalties have not been stringent enough and that the CRA statute enables the regulators to take a more aggressive stand on assessment areas. Superior, for example, received a low satisfactory rating on its lending test instead of being required to re-draw its assessment areas. Precedents established by the federal banking agencies provide reasonable expectations that the regulation and procedures regarding assessment areas can and must evolve with the changing nature of banking.

**Activities of Affiliates**

The CRA regulation must be changed to mandate that the CRA-related activities of non-depository affiliates of banks and thrifts be part of CRA exams. The current regulation makes it optional for banks to include the activities of their non-depository affiliates on the lending, investment, service and community development tests. This allows banks to "cherry pick" the activities of non-depository affiliates. Banks can choose to include affiliates when they are making safe and sound loans to LMI customers but exclude them when they are making predatory loans or primarily making loans to affluent customers. The optional inclusion of affiliates results in the manipulation of the CRA evaluation process and renders it less effective in ensuring that the credit needs of LMI communities are met. Furthermore, the business operations of banks and their non-depository affiliates are often intertwined. Not including the non-depository affiliates prevents examiners from scrutinizing fully how banks operate in LMI communities through their non-depository affiliates.

**Enhance CRA Rating Scheme and Public Improvement Plans**

To combat CRA grade inflation, low and high satisfactory ratings must be possible overall ratings on all CRA exams in addition to ratings on subsections of the exams. The CRA ratings have become less meaningful in recent years since less than 2 percent of banks and thrifts fail their exams. If low and high satisfactory were possible ratings, greater distinctions can then be made between banks' community reinvestment performance since CRA examiners can choose from six possible ratings instead of the current four ratings.

[6] See Appendix A to Part 228, Code of Federal Regulations, Title 12, Part 228.

Banks with low satisfactory ratings in addition to those with failing ratings must be required to submit a public improvement plan to the regulators regarding how they would improve their CRA performance. NCRC believes that the public improvement plan must be subject to a public comment period. Currently, banks failing their CRA exams must place a plan in their CRA public file, but no public comment period is required. Banks with low satisfactory ratings and those that fail need a higher level of public accountability as a spur for improving their performance. If regulatory agencies reviewed improvement plans and required banks to make warranted adjustments to their plans after the public comment period, the banks would be more likely to improve their reinvestment performance.

The federal banking agencies must also require public improvement plans in cases when a bank achieves a low satisfactory rating on its lending test on consecutive CRA exams or a low satisfactory rating on its lending test in a number of its assessment areas. The lending test must remain the primary test since redlining and predatory lending are still too prevalent in minority and working class communities. If a bank consistently receives a below average rating (low satisfactory or less) on its lending tests, it must be required to undertake the public process of submitting an improvement plan, receiving comments on the plan from the public, and waiting for approval of or adjustments to its plan by the federal regulatory agencies.

**CRA Enforcement Must be Strengthened**

The Gramm-Leach-Bliley Act (GLB) mandates that banks with failing CRA ratings cannot engage in mergers with non-bank financial institutions. The Federal Reserve has applied this statutory requirement only to the acquiring institution, not the "acquiree," although the GLB makes no such distinction. The federal banking agencies must end this inconsistency since passing CRA exams must be an incentive for banks that wish to be acquired as well as banks seeking to acquire other institutions.

Banks can "appeal" their CRA rating immediately after their exams. In a current case, staff with the Federal Reserve Bank of Cleveland informed NCRC that the appeals process was confidential, even when a community group has submitted a comment on a CRA exam. A few weeks later, NCRC learns via the trade press that the bank, WesBanco based in West Virginia, has appealed its Needs to Improve rating. Since the bank issued a press release about its appeal, NCRC questioned whether the process was confidential and consulted the "appeal" guidelines implementing Section 309 of the Riegle Community Development and Regulatory Improvement Act and the Federal Reserve Bank of Cleveland's guidelines. The guidelines for Section 309 do not establish a confidential appeal process. In fact, they allow Reserve Banks to solicit the views of other parties for rendering a fair decision, as the Federal Reserve Bank of Cleveland has done.

In the case of WesBanco, the bank has had a poor reinvestment record for several years. Before failing its present exam, the last CRA evaluation gave the bank a low satisfactory on the lending test and a needs to improve on the investment test. A "confidential" appeals process only serves to provide secret opportunities for poor performing banks to secure a passing rating and escape penalties for not meeting their CRA obligations. NCRC strongly believes that the federal banking agencies must clarify that the

appeals process is not confidential and that parties that have submitted comments on CRA exams will be invited to submit comments during the appeals process.

**Quantitative versus Qualitative Criteria**

**Emphasis on Quantitative Criteria is Appropriate and Does Not Cause Unprofitable Lending**

The emphasis on CRA exams must remain on quantitative criteria. Banker complaints about the quantitative emphasis are attempts to weaken exams and will ultimately make them less consistent. The quantitative measures such as portfolio share of loans or market share of loans compare banks against their peers operating in the same market. They are flexible and accurately reflect differences in markets or capacities of individual banks. For example, under the portfolio share measure, a bank will not be expected to make as high a percentage of loans to LMI borrowers in markets where the price of homes are high relative to income levels. Peer comparisons on CRA exams to all lenders in the market and/or lenders with similar asset levels will also reflect the high cost of housing in the particular market. In other words, all lenders and those with similar asset levels will likewise make lower percentage of loans to LMI borrowers in areas where the cost of housing is high.

Contrary to the assertions of some banks, the emphasis on quantitative criteria has not forced banks to make unprofitable loans in order to achieve a high volume of loans to LMI borrowers and communities. In their 1997 study entitled *Community Reinvestment and the Profitability of Mortgage-Oriented Banks*, Federal Reserve economists Glenn Canner and Wayne Passmore stated, "that we find no compelling evidence of lower profitability at commercial banks that specialize in home purchase lending in lower-income neighborhoods or to lower-income borrowers." They add that "Our regressions for the three years (1993, 1994, and 1995, which were years of high levels of CRA-related lending) suggest that the profitability of banks seems unrelated to, or perhaps slightly positively related to, the proportion of lending they extended in lower-income tracts."[7]

In 2000, the Federal Reserve released a survey on the profitability of CRA-related loans made by the nation's 500 largest banks as required by the Gramm-Leach-Bliley Act. This survey found that the great majority of banks reported CRA loans made to low- and moderate-income borrowers to be as profitable as their overall lending. Also, the CRA loans did not exhibit higher foreclosure rates.[8] Federal Reserve economists followed the release of this survey with a supplemental analysis showing that so-called marginal CRA loans were 3 to 5 times more likely to be reported as profitable as unprofitable.[9] These are loans that banks felt they had to make to earn a passing CRA rating. If these loans were highly unprofitable, CRA compelled banks to make bad loans. But, in fact, the reverse was true.

---

[7] Glenn Canner and Wayne Passmore, *The Community Reinvestment Act and the Profitability of Mortgage-Oriented Banks*, Finance and Economic Discussion Series, Federal Reserve Board, February 1997.
[8] *The Performance and Profitability of CRA-Related Lending*, Report by the Board of Governors of the Federal Reserve System submitted to the Congress pursuant to section 713 of the Gramm-Leach-Bliley Act of 1999, July 17, 2000.
[9] Robert B. Avery, Raphael W. Bostic, and Glenn B. Canner, *Assessing the Impact of CRA on Banking Institutions*, Division of Research and Statistics, Board of Governors of the Federal Reserve System, presented at the Federal Reserve's Second Community Affairs Research Conference, Mach 2001 in Washington DC.

**Specific Suggestions on How Qualitative and Quantitative Criteria Should be Used**

Qualitative criteria cannot be used to improve a failing performance or low satisfactory performance to higher grades on individual tests of the large bank exam or the other exams. Low satisfactory and failing ratings mean that lenders perform below average on the tests in question. Any innovative programs of these banks must be low volume. If their innovative programs were operating at a higher volume, their HMDA (Home Mortgage Disclosure Act) or small business data would show that they were out-performing their peers.

It is appropriate to use qualitative and "innovative" criteria to improve the rating of a bank performing in a satisfactory manner or in a high satisfactory manner. But considerable care must be made in these judgments so the CRA regulation must not prescribe how qualitative criteria should be used in these cases.

Qualitative criteria cannot penalize banks performing on a satisfactory or higher rating on any of the tests. For example, if a bank has a satisfactory level of investments (as measured by quantitative criteria), the rating on the investment test must be satisfactory. The bank in question may have a reasonable dollar amount of Low-Income Housing Tax Credit investments. This may meet an important investment need in a particular community. The bank should not fail its investment test because Low-Income Housing Tax Credits are not deemed to be innovative. The regulators should continue applying an existing Question and Answer (section .28-1) in the Interagency Q&A document that confirms that the innovative criteria will be used in this manner. The "innovation" criteria should reward new and creative products by possibly improving ratings, but should not be used to penalize banks if they are meeting lending, investment, and service needs by tried-and-true and effective techniques and products.

**Large Bank Exams**

**Weight of Tests**

The weight of the tests in the large bank exam must remain 50 percent for lending, 25 percent for services and 25 percent for investment. Lending is primary because a community cannot be revitalized if it receives investments and services, but discrimination in lending and/or a rise in predatory lending prevents homeowners and small business owners from receiving credit to buy, sell, and upkeep their homes and small businesses.

**Lending Test**

**How to Consider Subprime Lending**

Lending institutions must be encouraged to make as many prime loans as possible to LMI and minority communities. NCRC believes that the prime lending market is not saturated; that is, there are many more opportunities to lend to LMI and minority borrowers creditworthy for prime loans. The subprime

market suffers from widespread price discrimination and a segment of the market is predatory. Evidence of price discrimination indicates that thousands of borrowers stuck with subprime loans are creditworthy for prime loans.[10] The CRA regulations have an important role to play in increasing prime lending for underserved customers and in cleaning up the subprime industry.

When subprime lending involves price discrimination, the purpose of CRA to build wealth and meet credit needs is defeated.[11] As an example, suppose a borrower receives a subprime mortgage loan of $100,000 at a 9 percent interest rate and makes a downpayment of $5,000. If the borrower was actually creditworthy for a prime loan of 8 percent, he pays a "discrimination premium" of $24,480 over the 30-year life of the loan. If the borrower had received a loan with a 10 percent interest rate, his total payments would be $49,320 higher than they would be in the absence of price discrimination.[12] Thus, an overcharge of even one to two percentage points in interest results in the loss of a significant amount of equity, which could have been used to send a child to college and/or start a small business. A Freddie Mac economist estimates that 1 percentage point of the interest rate on the typical "A-" loan cannot be explained by risk.[13] While it cannot be explained by "risk," this price discrimination thwarts CRA's purpose of satisfying credit needs in a way that rebuilds the wealth of communities and families.

The lending test's qualitative factors relating to innovative and flexible loan practices must be further developed in the cases of subprime lenders. For example, consider the case of two lenders of similar asset size and range of loan products operating in the same metropolitan area. If one lender is making most of its loans with relatively high interest rates and fees to low- and moderate-income communities and borrowers, it should not receive as high a CRA rating as the other lender that is making mostly prime rate loans to these same communities. Clearly, the lender that is making prime rate loans has been more effective in figuring out how to apply flexible underwriting techniques to traditionally underserved borrowers. As well as considering interest rate and fees under the innovation criterion, quantitative measures must be developed that consistently assess loan costs of lenders operating in the same or similar assessment areas with comparable performance contexts and numbers of customers qualified for prime loans.

In order to perform a more sophisticated qualitative and quantitative analysis of subprime lending, the federal banking agencies must collect delinquency and default data by race and income level of neighborhood and borrower. Ideally, this data would become part of HMDA data, but it must at least become part of standard tables in CRA exams. A lender must score lower on the lending test if its

---

[10] Freddie Mac web page, http://www.freddiemac.com/corporate/reports/moseley/chap5.htm; "Fannie Mae Vows More Minority Lending," in the *Washington Post*, March 16, 2000, page E01. See also, Anthony Pennington-Cross, Anthony Yezer, and Joseph Nichols, *Credit Risk and Mortgage Lending: Who Uses Subprime and Why?*, Working Paper No. 00-03, published by the Research Institute for Housing America in September of 2000.

[11] The CRA statute does not explicitly refer to building wealth in LMI communities. However, meeting legitimate credit needs enables LMI borrowers to buy a house or start/expand a small business, thereby increasing their wealth.

[12] Calculations done by the mortgage calculator on Fannie Mae's Homepath web page, http://www.mortgagetoolshed.com/toolshed/tcc/signedhome.jsp?cid=homepath.

[13] Freddie Mac economist Peter Zorn's presentation at a forum on March 14, 2000 co-sponsored by the National Neighborhood Coalition and Freddie Mac.

**Test for Wholesale and Limited Purpose Institutions**

NCRC strongly believes that the test for wholesale and limited purpose institutions must not be applied to additional banks or thrifts. In particular, this test must not be applied to branchless and other non-traditional banks that offer bank services and loans on a nationwide basis. If the wholesale and limited purpose test is applied to these institutions, the institutions will be subject to a test that only measures their level of community development lending, investing, and service. The test will not investigate the numbers of home mortgage loans, small business loans, or deposit accounts provided to LMI customers. The resulting exams would be directly contrary to the purpose of the CRA statute to ensure that a bank is safely and soundly meeting credit and deposit needs of all the communities in which it is chartered.

With the advances in computers and industry software such as CRA Wiz™ and HMDAWare™, it is a relatively straightforward task to list the metropolitan areas and non-metropolitan counties in which non-traditional lenders make a substantial number of their loans and collect their deposits. Then, examiners can apply NCRC's recommendations concerning assessment areas so that the great majority of a branchless bank's loans are included on its CRA exam. The wholesale and limited purpose exam must not become a lazy and sloppy method for assessing non-traditional banks, especially since alternative procedures can make sure that these banks are rigorously examined.

Presently, some banks and thrifts inappropriately qualify for the limited purpose and wholesale test. The Federal Reserve Bank of Boston, for instance, recently examined the Boston Safe Deposit and Trust Company under the limited purpose and wholesale test in October of 2000. The exam indicates that this institution is "primarily a fidcuciary bank offering custody and asset management services...for high net worth individuals." The exam then discusses that the bank recently ceased its jumbo mortgage operations, but has a loan officer dedicated to affordable home mortgage lending programs.[26] The exam does not review the bank's HMDA data, which provides strong indications that lending is not an incidental activity. During 1999, the bank made 2,092 loans, but only issued 1.3 percent of its loans to Blacks and 3.5 percent of its loans to LMI borrowers. The exam mentions 104 loans made to LMI borrowers by its bank and its affiliate (this is close to the 74 loans reported as originations in the HMDA data for 1999). The FDIC web page reports that single-family lending constituted a significant 37 percent of the bank's assets as of March 2001 and 47 percent as of March 2000. For Boston Safe Deposit and Trust Company, the limited purpose designation and its "outstanding" CRA rating masks limited service to LMI borrowers.

An even more questionable assignment of "wholesale" status is the Office of Thrift Supervision's designation of this status to Ocwen Federal Bank in June of 2001. The previous CRA exam dated June 1999 did not adequately examine the lending and purchasing activity of this subprime institution.[27] Even though loan purchases accounted for 72 percent of the loans reported under HMDA, the examiner focused on loan originations only. Ocwen is nationally known as an institution that purchases "non-

[26] CRA evaluation of Boston Safe Deposit and Trust Company, Docket Number #44602, Federal Reserve Bank of Boston, October 30, 2000.

[27] CRA evaluation of Ocwen Federal Bank, FSB, Docket Number # 04592, Office of Thrift Supervision, Northeast Region, June 21, 1999.

delinquency and default rates are significantly higher than its peers by race and income level of neighborhood and borrower.

To increase incentives for lenders to make prime loans, prime lending must receive more weight on CRA exams, particularly for banks that engage in both prime and subprime loans. Prime and subprime loans must be evaluated separately just like home mortgage, refinance, and home improvement lending are currently. In order for a bank that offers both prime and subprime lending to pass its lending test, it must receive at least a satisfactory rating on the prime portion of its test. This proposal is similar to the requirement that a bank must receive at least a low satisfactory on the lending test to pass its CRA exam. But it would put more weight on the prime portion of the lending test since the lender would have to perform in a satisfactory manner on that part of the test, not merely in a low satisfactory manner.

The Federal Reserve's proposal to include APRs (Annual Percentage Rates) on HMDA data must be enacted and the data must include separate data on fees. Only then, can CRA examiners consider prime and subprime lending separately on exams. HUD's (Department of Housing and Urban Development) list of subprime lenders is valuable, but it misses a considerable number of supbrime loans by so-called prime specialists (those lenders whose prime loans constitute more than 50 percent of their loan portfolio but who still make a considerable number of subprime loans).

A regulatory requirement must stipulate that CRA exams must occur concurrently with fair lending and safety and soundness exams. The Office of the Comptroller's decision to conduct fair lending exams less frequently than CRA exams must be reversed. In order to abide by the CRA statutory requirements for safety and soundness, subprime loans must be judged to be safe and sound in order to receive any credit. Also, NCRC applauds the new Question and Answer in the Interagency CRA document that penalizes banks on CRA exams for making loans that violate the anti-predatory provisions of HOEPA, TILA, and other federal statutes. Lenders must also be penalized for violations of local and state anti-predatory and anti-payday lending statutes. This Q&A must be moved to the regulation itself. Reverse redlining, or steering low- and moderate-income or minority borrowers to over-priced loans (interest rates and fees in excess of risk) must also be severely penalized on CRA exams.

**Minorities Need to be Explicitly Considered on the Lending Test**

The CRA regulations must require lending to minority individuals and communities to be explicitly considered in a manner similar to lending to LMI individuals and communities on the lending test. Subprime lenders have dominated refinance and home equity lending in minority communities during recent years. HUD has documented that borrowers in black neighborhoods are five times more likely to receive subprime refinance loans than borrowers in white neighborhoods.[14] In testimony this summer to the Senate Banking Committee, NCRC revealed that minority neighborhoods in Trenton are four times

[14] Department of Housing and Urban Development, *Unequal Burden: Income and Racial Disparities in Subprime Lending in America* (April 2000, www.hud.gov/pressrel/pr00-75.html).

more likely than white neighborhoods to receive subprime refinance loans.[15] NCRC also found that middle-income blacks in the District of Columbia are eight times more likely to receive subprime refinance loans than middle-income whites.[16] Differences in creditworthiness between Black and white communities do not explain all of this disparity. Price discrimination is also occurring. CRA exams have the potential to reduce the incidence of price discrimination and the lending disparities.

If the regulators include lending to minorities and adopt comprehensive reforms regarding the treatment of subprime loans on CRA exams, NCRC believes that prime lending will rise in minority communities and crowd out predatory lending. CRA exams must also consider lending to minority-owned businesses because predatory lenders have made abusive refinance and home equity loans to minorities seeking to start their businesses (see below for necessary data enhancements to the CRA small business data).

The CRA statute states that banks must serve "the credit needs of the local communities in which they are chartered."[17] This does not limit CRA exams to examining lending to low- and moderate-income borrowers and communities. In fact, this mandate obligates federal banking agencies to ensure that traditionally underserved minority communities do not fall victim to redlining and predatory lending.

**Should Purchases Count?**

Originating loans is more difficult than purchasing them. Loan originations must be examined separately from loan purchases and must receive more weight. NCRC proposes that a lender must perform in at least a satisfactory manner on the portion of the test that considers loan originations in order to pass its lending test.

Lending institutions have told NCRC about the manipulative practice of some of their peers buying many loans made to LMI borrowers and communities just before their CRA exams. This manipulation would stop if the federal banking agencies consider purchases in the manner suggested by NCRC.

Lenders must face stiff penalties on CRA exams if they purchase predatory loans that strip equity from borrowers.

**Investment Test – Should it Remain or be Replaced by a "Community Development Test"**

The investment test must remain separate because pressing needs for investments exist in low- and moderate-income communities. Federal Reserve Chairman Alan Greenspan, for example, stresses the need for greater equity investment in small businesses.[18]

---

[15] Testimony of the National Community Reinvestment Coalition before the Committee on Banking Housing and Urban Affairs, U.S. Senate Hearings on Predatory Mortgage Lending, Friday, July 27, 2001, see http://www.ncrc.org for a copy of the testimony.
[16] See NCRC Subprime Lending Analysis: Washington DC and the Surrounding Metropolitan Area, 1998 in the press releases section for year 2000 on NCRC's web page.
[17] 12 USC 2901; Title VII of Pub. L. 95-128, 91 Stat. 1147 (October 12, 1977)
[18] Remarks by Chairman Alan Greenspan, *Changes in small business finance*

Occasionally, banks feel that they must structure a community development loan as an investment because they need to increase the number of investments to earn a good rating on their investment test. NCRC understands that converting community development loans into investments is not optimal in terms of efficiency. In these situations, the financing should remain as community development loans, but the bank should have the discretion to consider these as qualified investments for CRA test purposes.

In return for providing flexibility regarding community development lending, NCRC insists that the investment test become more rigorous by consistently applying a quantitative benchmark such as a ratio of community development investments to bank assets. The ANPR repeats complaints by banks that investment opportunities are limited in some geographical areas and that smaller institutions have difficulty competing for investments because larger ones can offer better deals on the investments. The ratio of investments to assets allays such concerns because it can be used to compare banks against each other in the same market and of similar asset sizes. Also, the ratio would add needed rigor to the investment test. Many CRA exams simply list investments and do not provide much discussion and/or quantifiable benchmarks indicating if the level of investments is reasonable.

In general, CRA examiners do not differentiate among types of investments or award more points to those that have the most benefit to low- and moderate-income communities. A criterion of the investment test measures the "responsiveness of investments to credit and community development needs." Rarely, does a CRA exam contain careful judgments or data analysis quantifying how many residents of low- and moderate-income communities will receive jobs or housing as a result of an investment. Those investments that maximize job and housing creation for low- and moderate-income residents in low- and moderate-income communities are the most responsive to community needs.

In the case of two banks of similar asset size, the bank making investments which benefit the most LMI individuals and communities should receive more points on the "responsiveness" criterion. CRA exams rarely contain this type of comparison among peer banks.

Similarly, the CRA examiners do not differentiate among types of investments or consider the extent to which investments are not routinely provided by the private sector. Long-term investments with below market rates of return or grants to nonprofits are scarcer than investments in municipal bonds. CRA exams could readily incorporate ratios that compare grants as a percent of bank assets and ratios that compare the percent of difficult and "patient capital" investments as a percent of bank assets. Along with meaningful information on the extent of targeting of low- and moderate-income communities, this additional data would make the exams more rigorous and consistent in their judgments of bank performance.

at the Federal Reserve System Research Conference on Business Access to Capital and Credit, Arlington, Virginia, March 9, 1999, http://www.federalreserve.gov/boarddocs/speeches/1999/19990309.htm, Chairman Greenspan states that, "Continued efforts to develop the markets for private equity investments will be rewarded by an innovative and productive business community. This is especially true in lower-income communities, where the weight of expansive debt obligations on small firms can severely impede growth prospects, or more readily lead to business failures."

Banks and thrifts must be severely penalized on CRA exams if they make any investments in predatory lenders or other entities that exploit low- and moderate-income communities.

**Service Test**

NCRC believes strongly that the service test must become more rigorous. Dr. Michael Stegman and his colleagues with the Center for Community Capitalism at the University of North Carolina find troublesome evidence of grade inflation on the CRA service test. Their regression analyses of more than 2,000 large bank exams indicate that banks in danger of failing their CRA exams (those with low satisfactory on the lending test and needs to improve on the investment test) have a much higher probability of scoring higher on the service test than banks that have failed their lending and investment tests. In other words, it was much more likely for a bank in danger of failing to receive a good score on the service test than a bank that was clearly failing its CRA exam. Stegman's review of CRA exams revealed that some banks on verge of failing did legitimately step up their service activities while others had poor service records.

In order to reduce the chances of inflation on the service test, NCRC asserts that the federal banking agencies must mandate additional data collection for deposit and checking accounts as well as more data on service fees, alternative service delivery channels, and community development services. The service test will become more objective and consistent with the additional data.

**Data Must be Required on Savings and Checking Accounts**

The federal banking agencies must require banks to disclose data on the distribution of checking and savings accounts by the race and income level of the borrower and census tract. In the previous regulatory changes of 1995, the agencies decided against this due to the cost of collecting the data. Technology has progressed rapidly since then. In particular, as long as banks have the street addresses of account holders, they can apply "geo-coding" software to translate the street addresses to the census tract location of the account holders. Any added cost borne by the banks would be outweighed by the public benefits of this data, as well as valuable information for the banks on their position in the market for deposits. It is becoming much more difficult to measure how well banks are providing services in the absence of basic information on checking and savings accounts.

At this point, branch presence is one of the primary means by which bank delivery of services is measured on the service test since data on branches is one of the only pieces of data available to federal banking agencies. If data becomes available on the distribution of savings and checking accounts, CRA examiners (and the general public) could use their discretion about whether a relatively low percentage of branches in LMI census tracts could be compensated by an above-average percentage of checking and savings accounts in LMI tracts and to LMI borrowers.

While a good distribution of accounts is desirable, bank branches must remain an important criterion on the service test since branch presence is still the primary method LMI customers use to access a bank. In particular, NCRC agrees with the recommendation of Professor Stegman that branch distribution be

compared against the percentage of households in low- and moderate-income census tracts. Branch presence in residential neighborhoods (as measured by tracts with higher percentages of households) remains imperative for serving LMI customers. Often, check cashers and other fringe bankers in inner city neighborhoods are open long after the end of the workday. Measuring branch presence in LMI neighborhoods encourages banks to take advantage of the profitable opportunities to serve the high demand for banking needs and compete against the fringe bankers.

**Cost of Services**

The costs of services must be a factor on the service test because high fees on banking products defeat CRA's purpose of meeting deposit needs that build wealth in LMI communities. High fees drain wealth of consumers and prevent them from accumulating savings for downpayments on mortgage loans or establishing collateral for small business loans. A recent Fannie Mae Foundation report presents a powerful example of check cashing and bill paying fees costing a low-income borrower up to $500 per year at a non-bank, "fringe" institution. In contrast, banks charge between $30 to $60 dollars for these services. If a low-income customer used the bank, she could save up to $500 per year. If she invested this amount at an interest rate of 4 percent, she would accumulate up to $6,000 after ten years, enough for a downpayment on a mortgage loan.[19]

High fees for services also reduce access to the bank products for LMI and minority customers. If a lending institution assesses a fee for using tellers but provides Internet and other electronic services free of charge, this is a form of price discrimination that disproportionately affects LMI and minority customers. A recent Census Bureau survey confirms that affluent households are four times more likely to have access to the Internet than low-income households.[20]

Lenders with high fees exhibiting disparate impacts must receive lower points on the service test under a new "cost and accessibility" portion of the test. In addition, if two similarly situated lenders offer similar amounts of bank checking and savings accounts to borrowers, but one lender charges significantly higher fees, the higher cost lender should receive fewer points on the CRA service test. High fees are contrary to the purpose and spirit of CRA in promoting accessibility to bank products and wealth-building in LMI communities.

Payday lending must not receive any credit on CRA exams. Alternative products exist to short-term and usurious payday loans. These products include credit cards (secured and unsecured) and checking accounts with overdraft protection. Individual Development Accounts could also be used to fund emergency loans.

In September of 2000, the Office of Thrift Supervision gave Crusader Savings Bank a needs-to-improve rating, in part because the thrift engaged in abusive payday lending. The OTS exam stated that

[19] James H. Carr and Jenny Schuetz, *Financial Services in Distressed Communities: Framing the Issue, Finding Solutions*, Fannie Mae Foundation, August 2001.
[20] Eric Newburger, *Home Computers and Internet Use in the United States*, Current Population Reports of the U.S. Census Bureau, issued September 2001.

Crusader's payday loans had Annual Percentage Rates (APRs) up to 431 percent and consume 80 percent of a borrower's bi-weekly income. The examiner concluded that "the institution's participation in this type of credit practice was considered an adverse factor...in the overall CRA rating."[21]

In contrast, the Office of the Comptroller of the Currency (OCC) awarded Eagle National Bank with Satisfactory ratings, despite that fact that Eagle made more than 600,000 payday loans.[22] Unlike the OTS exam, the OCC evaluation did not probe into the wealth-depleting nature of payday lending.

The ultimate test is whether payday loans are comparable in price to other products offered by banks. Payday loans flunk this test by wide margins. Therefore, payday lending must not be counted on CRA exams and must be penalized in most cases, since most payday lending resembles the lending done by Crusader.

**Alternative Delivery Systems**

CRA examiners do a poor job of applying the criterion of alternative delivery systems on the service test. Banks claim credit for banking by phone, banking at work, and internet banking while most exams do not scrutinize how many low- and moderate-income borrowers use these services. If banks wish to receive credit for these delivery systems, they must provide examiners with data on the distribution of use by income level of borrower and census tract. A comprehensive analysis of CRA service tests by the Center for Community Capitalism finds that only the Office of the Comptroller of the Currency requires data from banks on the number and percent of LMI customers using alternative delivery systems.[23] Examiners must then compare this data against the distribution of other bank services by income level. Examiners must also compare this data on utilization of alternative services against peer banks.

**Community Development Services**

This is also a weak portion of the service test. Often, CRA exams list community development services without describing the breadth or depth of these services. The federal agencies should establish expectations that banks will receive more points on the community development portion of the service test if banks present data on the numbers of LMI and minority consumers financial counseling sessions or other community development services reach. Data on the outcomes, including the percent of customers attending counseling who later opened accounts, should also be provided. CRA exams must

---

[21] CRA Performance Evaluation of Crusader Savings Bank, FSB, Docket #05030, Office of Thrift Supervision Northeast Region September 11, 2000.
[22] CRA Performance Evaluation of Eagle National Bank, Charter Number 21118, Office of the Comptroller of the Currency, Philadelphia Field Office, May 5, 1999 and see April 1998 exam.
[23] Dr. Michael A. Stegman, Kelly Thompson Cochran, and Robert Faris, *Creating a Scorecard for the CRA Service Test: Strengthening Basic Banking Services Under the Community Reinvestment Act*, a working paper published by the Center for Community Capitalism at the University of North Carolina at Chapel Hill. Dr. Stegman and colleagues presented findings of the paper at a focus group session convened by NCRC in late June of 2001.

make comparisons among peer banks of the numbers of LMI and minority consumers receiving community development services.

The ANPR states that some banks believe that the small amount of points on the service test does not provide much incentive for providing community development services, which can be labor intensive. The primary emphasis on the service test must be on the provision of bank accounts and the availability of branches to LMI customers. Retaining this emphasis does not dissuade banks from providing community development services, but encourages banks to design these services so they are most effective in enabling people to open accounts and/or enter the banking system.

**Services for the Unbanked**

Services offered to the unbanked such as check cashing should receive points on the service test, especially if the bank is effective in bringing the unbanked into the banking system. Partnerships with check cashers should not count on the service test because the aim of the service test should be to encourage banks to offer low-cost alternatives to the fringe banking system. At the very least, partnerships with check cashers should count only if the check cashing fees have been reduced significantly. The current monopoly that check cashers enjoy in too many minority and low- and moderate-income neighborhoods result in above-market, exorbitant prices.[24] CRA exams must be used to in a way that breaks up these neighborhood-level monopolies and eliminate the wealth transfers from unbanked customers to check cashers and other fringe bankers.

**Community Development Activities**

The ANPR alludes to suggestions to combine community development services with community development loans and investments to form a new test considering the three types of community development activities. NCRC believes that community development services should remain as part of the service test because community development services, such as financial literacy, prepare consumers to take advantage of bank services. They are not similar to community development investments or community development loans. As mentioned earlier, NCRC proposes that banks be allowed more discretion in deciding whether to place community development loans in their lending or investment tests.

The definition of community development must be more targeted to LMI communities. Specifically, the current definition includes "activities that promote economic development by financing small businesses and farms." This overly broad definition can qualify investments in Small Business Investment

[24] Gregory Squires and Sally O'Connor, *Fringe Banking in Milwaukee: The Rise of Check-Cashing Businesses and the Emergence of a Two-Tiered Banking System,* in Urban Affairs Review, Vol. 34, No. 1, September, 1998. A key finding was that in African-American communities, there was one bank for every check-cashing business compared to 15 banks for each check-cashing business in white areas. In *Reinvestment Alert* Number 10 of March 1997, the Woodstock Institute finds that in minority and low-income neighborhoods in Chicago, check-cashing outlets outnumber bank branches by a ratio of 12 to 1. They also calculate that the cost of cashing one check at a check-cashing outlet is equivalent to the monthly cost of a bank checking account.

Corporations (SBICs) that do not benefit low- and moderate-income neighborhoods. This part of the definition must be narrowed to include only economic development and financing of small businesses and farms that are located in low- and moderate-income communities and/or mostly employ low- and moderate-income persons. Community development must not include any activities such as establishing liquor stores or payday lenders that harm low- and moderate-income communities.

The ANPR asks if large banks should receive credit for community development activities in any part of the country, not only in a regional or statewide area that includes their assessment area. NCRC believes this would further divert banks' attention away from their assessment areas. Instead, reforms should be made to assessment area procedures that result in assessment areas covering most of a bank's lending, investment, and service activities (as described above).

**Small Bank Exams**

NCRC opposes vigorously suggestions that the asset level qualifying for the small bank exam be raised above $250 million in assets. Instead of additional banks qualifying for the streamlined small bank exam, banks with assets less than $250 million must be expected to demonstrate a record of providing investments and services as well as lending to LMI and minority communities.

According to the most recent data (1st quarter 2001) on the FDIC web page, about 7,500 or 76 percent of the banks and thrifts in this country have assets less than $250 million and therefore qualify for the small bank exam. If the asset level for qualifying for the small bank exam is raised to $500 million, an additional 14 percent of the banks and thrifts would qualify, meaning that about 90 percent of depository institutions would be subject to a streamlined test only once every four or five years. If the asset level is raised to $1 billion dollars, an additional 4 percent of depository institutions would enjoy the streamlined test.

Contrary to the assertions of some banks, evidence exists that institutions with assets under half a billion dollars have the financial capacity to invest in and provide services to LMI communities. The FDIC web page, for example, indicates that depository institutions with assets between $300 to $500 million have 9.8 percent of their assets invested in equity capital. This is a higher level than the 8.6 percent for all banks and thrifts. Likewise, institutions with assets between $100 to $300 million also committed about 9.8 percent of their assets in equity capital. Institutions with assets under $100 million had 11.2 percent of their assets in equity capital. The data strongly suggests, therefore, that institutions with assets of $300 to $500 million as well as smaller banks have the capacity to make community development investments.

Instead of qualifying more institutions for the streamlined small bank exam, the federal banking agencies must expect institutions with assets less than $250 million to demonstrate sufficient levels of investment and services. An investment and service test should be added to the small bank exam. At the very least, a small bank with assets under $250 million cannot earn more than a Satisfactory rating overall if they cannot demonstrate a Satisfactory or higher level of investments and services.

Smaller banks predominantly serve non-metropolitan and rural areas in which consumers confront fewer choices for their banking needs. Many rural counties have only one or two banks with branches. These banks enjoy a near monopoly, at least in terms of branches, which is the predominant means by which LMI consumers access banks. CRA regulations and exams must ensure that the smaller banks are providing a sufficient amount of affordable loans, services, and investments that serve as alternatives to predatory or payday lending.

Rural Vermont illustrates the importance of rigorous CRA exams for smaller banks. In the county of Essex, Vermont, only one bank serves 6,459 people. This bank, the Community National Bank, has not been examined by the Office of the Comptroller of the Currency since 1995 according to the OCC and the FFIEC web sites. In the absence of CRA enforcement, rural banks with no local competitors have few incentives to provide an adequate level of affordable loans and services to low- and moderate-income borrowers. Grand Isle County, which is home to 6,901 people, only contains two banks. One bank, Merchants Bank, has $670 million in assets and made $13 million in equity investments supporting more than 600 units of affordable housing. If the current small bank exam is applied to banks above $250 million in assets, the chances of banks like Merchant continuing this level of investment in underserved communities is seriously diminished.[25]

NCRC urges the regulators to strengthen the CRA regulation and examination procedures for small banks. While small banks have recently won regulatory concessions from Gramm-Leach-Bliley in particular, there is a good deal of evidence that small banks' records of meeting the credit needs of their communities are often inadequate. Virtually all of the "Needs to Improve" and "Substantial Non-compliance" CRA ratings in recent years have gone to banks with less than a billion dollars in assets. Even though they are examined with less rigor, banks examined under the small bank CRA exam have accounted for more than their share of less than satisfactory CRA ratings. A review of small bank CRA exams will show that banks with loan to deposit ratios as low as 40 percent, and sometimes even lower, regularly receive satisfactory CRA ratings. Even in states in which the average loan to deposit ratios for banks are in the 80 to 100 percent range, 40 and 50 percent loan to deposit ratios are almost always described by examiners as "reasonable" without any evidence of extenuating circumstances provided.

In order to lessen the tendency of CRA examiners towards "grade inflation," NCRC proposes that the regulators establish more objective criteria in the small bank exam. For example we would propose that small banks with a loan to deposit ratio that is less than 75 percent of their state average be assumed to have less than satisfactory CRA ratings unless specific extenuating circumstances are documented in the CRA evaluation. Specific benchmarks would make CRA evaluations more objective and less subject to grade inflation even if examiners retained some flexibility to deal with individual circumstances.

[25] CRA Performance Evaluation of The Merchants Bank, Certification Number 6268, Federal Deposit Insurance Corporation, January 10, 2000.

performing" or seriously delinquent loans. Many consumers, including some that have been represented by NCRC, have filed suit against Ocwen for its "collection" practices on delinquent loans. The previous CRA evaluation did not examine if Ocwen's collection practices served credit needs and helped neighborhood revitalization efforts or if Ocwen destabilizes neighborhoods by forcing consumers into foreclosure. When Ocwen is examined under its next CRA exam as a "wholesale" institution, the CRA exam will not investigate the impacts of Ocwen's lending and purchasing activities on LMI and minority communities.

Since some lending institutions and regulatory officials currently abuse the limited purpose and wholesale designation procedures, any further relaxation of the procedures would only invite further abuse and evasion of the CRA obligation to serve the credit needs of all communities. In fact, the designation procedures need to be strengthened. Presently, the federal banking agencies consider requests for limited purpose and wholesale designations for a period of three months. The agencies must also request public comments on these requests and must send a copy of these requests to parties that have previously commented on the CRA performance of the institutions in question. If a federal banking agency proceeds to designate an institution as a limited purpose or wholesale institution that makes a considerable number of loans, the agency must still apply the lending test of the large bank exam to the institution in addition to the community development test.

**Strategic Plan**

The strategic plan should be eliminated. It has been abused too often; banks declare easy goals and examiners approve these goals.

In a strategic plan approved by the OTS, for example, Household, FSB proposed that 4 to 7 percent of its secured home equity loans and between 20 to 30 percent of their unsecured home equity loans would be made to LMI borrowers under their affinity lending program with the AFL-CIO. The OTS CRA exam confirmed that Household met these goals, but it did not explore whether these percentages were higher or lower than similarly-situated home equity lenders or whether the home equity loans of this subprime lender were made in a safe and sound manner. Also, the exam did not investigate why the percentage goal for secured home equity loans was much lower than the goal for unsecured loans. The exam also confirmed that Household far exceeded its dollar goal of making $50 million in loans to LMI borrowers in Illinois, Delaware, and Florida. The exam, however, does not investigate if the dollar level of lending was actually higher or lower than in previous years. While NCRC appreciates that Household's national goals for its AFL-CIO program implicitly acknowledged that it had to demonstrate adherence to CRA beyond a few assessment areas since it was a nationwide lender, neither Household nor the CRA examiner established that the goals were rigorous or even reasonable.[28]

If the federal agencies retain the strategic plan, they must require meaningful goal development. Banks' presentations of only the number and dollar value of loans, investments, and services will not suffice

[28] CRA evaluation of Household Bank, FSB, Docket Number 06194, January 24, 2000, Office of Thrift Supervision Central Region.

since these numbers have little meaning without any context. For example, when the bank lists the number of loans it will commit to in future years, is the percent of loans to LMI borrowers and communities higher or lower than in previous years? How does the percent compare with all lenders in the assessment area(s) and peer lenders? Is the bank's market share of loans to LMI borrowers and communities higher or lower than the bank's market share of loans to MUI (middle- and upper-income) borrowers and communities? Portfolio and market share measures must be the part of every strategic plan submission. Otherwise, the potential for abuse is too great.

During the public comment period on a strategic plan, the bank must explicitly respond to public comments on the plan, and the public must have a chance to respond to bank comments on their comments. Presently, the opportunity to respond to a bank's comment is not available or is limited due to the scanty nature of the data presented by the bank on its goals.

**Performance Context and Public Input**

When CRA examiners call a community group to ask for input, they must always inform the community group of the bank(s) that are about to be examined. In years past, NCRC members have commented upon instances in which an examiner will not divulge the name of the bank being examined. Community groups cannot provide meaningful input when the names of the institutions are withheld.

CRA examiners also cannot rely upon the input of community group contacts that are provided to them by the banks being examined. To make sure they are receiving the complete picture of the bank's performance, CRA examiners must make serious efforts to sample a variety of perspectives and use a variety of resources such as national and local coalitions of community groups to obtain diverse input.

An aspect of community group input that is often overlooked on CRA exams is measuring how responsive banks are to credit, investment, and service needs. Community development corporations and local public agencies have considerable experience and knowledge of which institutions respond to needs for investment capital and which do not. They will also have partnerships that involve loan products or low-cost savings and checking accounts. CRA exams, rarely if ever, include adequate community group contacts regarding the responsiveness as well as the quantity of bank's lending, investment, and service activities in traditionally underserved neighborhoods.

**Improving CRA Data Small Business Data**

As stated above, the Federal Reserve Board must adopt its proposal to enhance HMDA data to include the APRs and fees so that CRA examiners will be able to separately analyze prime and subprime lending.

The Federal Reserve Board must lift its Regulation B prohibitions on the reporting of race and gender of the small business owner. NCRC believes that race and gender reporting must be mandatory for small business data. Confronted with few choices for obtaining credit, minority small business owners have

been victimized by predatory lenders.[29] CRA exams must therefore scrutinize if minority-owned small business owners receive an adequate share of banks' small business loans.

Instead of only two categories (less and greater than $1 million in revenues), the specific revenue size of the business borrower must be included in the CRA small business data. The small business data for 2000 became less reliable on capturing loans to small businesses with revenues less than $1 million dollars since a much higher percentage of lenders indicated that they did not know the revenue size of the small business.[30] The current policy of allowing lenders to not report the revenue size of the small business if they did not use revenue size in making the loan decision must be discontinued.[31] Otherwise, CRA examiners will not know how many of the smallest businesses lenders are reaching.

The CRA small business data must include action categories that are similar to the action categories in HMDA data (which are applications, approvals, denials, withdrawn, incomplete, and approved not accepted). CRA and fair lending enforcement is rendered more difficult when no data exists on how the applicant was treated prior to the loan approval stage. Further, the small business data must report originations separately from renewals and refinances since these loan purposes serve significantly different credit needs.[32] Likewise, a data field should be added that indicates whether the small business loan was a credit card loan or a regular loan.

When HMDA data was improved in 1990, banks significantly increased their loans to traditionally underserved populations because they became more accountable for lending to these borrowers. The same phenomenon would occur if the federal banking agencies enhanced the quality of small business data.

**Data on Community Development Loans and Investments**

The current community development lending data reported under CRA is not very useful. It should be reported on the census tract level, not only the "aggregate" level. The purpose of the loan must also be reported, using categories of affordable housing, economic development, loans for social service facilities, and other common categories of community development loans. Loans for investments should likewise be reported on a census tract level. The purposes of investments must also be recorded including grants for community development organizations.

---

[29] NCRC has filed a HUD complaint for a minority-owned small business in the District of Columbia. The complaint number is 03-01-0448-8 and involves Ocwen Federal Bank.

[30] FFIEC Reports - Findings from Analysis of Nationwide Summary Statistics for 2000 CRA Data Fact Sheet (July 2001), see FFIEC web page, http://www.ffiec.gov/hmcrpr/cra_fs00.htm

[31] See the Interagency Question and Answer document, Section _*.42(a)(4)*_2.

[32] Section *.42(a)*-5 of the Interagency Q&A allows an institution to report one renewal or refinancing annually as a small business loan origination.

NATIONAL COMMUNITY REINVESTMENT COALITION NCRC

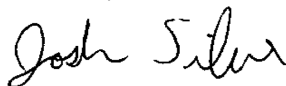
**Conclusion**

NCRC believes that our suggestions for updating the CRA regulation will produce CRA exams that are rigorous, performance-based, more consistent, and that are better able to capture the lending, investment, and service activity of rapidly changing banks and thrifts. These recommendations lead to enhanced enforcement of CRA.

This review of the CRA regulations is so vital that we urge the federal banking agencies to hold hearings around the country when they propose specific changes to the CRA regulation. It is vital that the agencies hear the diverse voices of America's communities as they consider a regulation that ensures that community credit needs are being met.

On behalf of NCRC's 800 member organizations (a roster is attached), we thank you for consideration of our comments in this matter critical to the wealth and economic chances of minority and working class communities.

Sincerely,



Josh Silver
Vice President of Research and Policy