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

Re: Docket No. 2001-49, Advanced Notice of Proposed Rule Making Regarding the Community Reinvestment Act of 1977

To the Chief Counsel's Office:

This letter is written in response to the federal bank and thrift regulatory agencies' request for comments on an advance notice of proposed rulemaking (ANPR) regarding the Community Reinvestment Act (CRA). The CRA regulations were revised in 1995. At that time the federal agencies committed to reviewing the revised regulations in 2002 to determine whether they met the goal of producing more objective, performance-based CRA evaluations. The agencies are seeking comment to determine whether and to what extent the regulations should be amended to better evaluate the performance of financial institutions under CRA.

The Massachusetts Division of Banks (Division) is the primary regulator for over 300 state-chartered banks and credit unions in the commonwealth. The Division is responsible for conducting financial safety and soundness, consumer compliance, community reinvestment act compliance, electronic data processing, and trust examinations of these institutions. The Division also is charged with licensing and examining over 3,000 non-bank financial entities, including mortgage lenders and brokers, check cashers and sellers, collection agencies, foreign transmittal agencies, finance companies, and small loan companies. These entities are also regularly examined for financial safety and soundness and compliance with various consumer protection laws and regulations.

The Commonwealth of Massachusetts is one of three states that actively examines financial institutions for compliance with community reinvestment on the state level. Massachusetts currently has its own CRA statute (M.G.L. c. 167, §14) and implementing regulation (209 CMR 46.00) that is substantially similar to the federal CRA regulation. The two most significant distinctions are that 1) the Massachusetts CRA uses a fifth composite rating category of "High Satisfactory" and 2) the Massachusetts CRA is applied to state chartered credit unions. In order that Massachusetts-chartered institutions are not subject to two different sets of requirements, the Division has worked to ensure that the Massachusetts CRA regulation remains relatively consistent with the federal CRA regulation. I would like to offer the following comments relative to the federal CRA.

Payday Lending

Currently neither the CRA regulation nor the current Q & A on the CRA regulations make any specific stipulation on the treatment or level of consideration given to payday lending activities during the CRA examination process. Payday lending has become a growing activity over the last several years. With payday lending borrowers pay a fee to receive an advance against their next paycheck. The premise is that the borrower will pay back the money from the proceeds of their next paycheck. Paying back the funds is typically accomplished by presenting the lender with a post dated check or by authorizing the lender to charge a bank account on a pre-determined date. If the borrower is unable to pay back the loan by the specified date he can pay an additional fee to extend the term of the loan. The Division has determined that payday lending in Massachusetts requires a license under the Division's small loan statute (M.G.L. c. 140, §96-114A) and its implementing regulation (209 CMR 12.00). Because small loan lenders in Massachusetts are limited in the rate of interest that they can charge for loans, payday lenders that wish to operate directly in Massachusetts would not be able to legally charge the typical high rates associated with this type of lending. However, the Division is aware of the growing practice of out of state banks offering payday loans through third parties (i.e. "charter renting") and claiming exemptions from usury limits by exporting the interest rate of the bank's home state. It is the belief of the Division that those financial institutions which engage in payday lending are working against the intent and spirit of the Community Reinvestment Act by providing credit at exorbitant and unconscionable rates most often to those in desperate situations who can ill afford to pay such high fees. If an individual must resort to borrowing money at interest rates exceeding 100% then there are most likely other issues going on regarding credit and budgeting that need to be addressed. If an institution has identified a need for small loans for short terms, it should look for ways to provide this service in a less costly manner. Further, the institution should also give strong consideration to providing consumer education programs which would help prevent individuals from being in a financial situation where their only course of action is to resort to a payday loan.

The Division is troubled when it sees financial institutions engaging in payday lending, particularly in an area or state where they do not otherwise conduct business. The Division questions an institution's level of commitment in meeting the needs of low and moderate-income individuals when it chooses to engage in an activity that takes unfair advantage of people. The Division strongly believes that the CRA regulations should include provisions for considering an institution's participation in payday lending or other activities, whether conducted inside or outside of the institution's assessment area when evaluating overall CRA performance. Further, the Division believes that those institutions that chose to "rent" their charters to entities that engage in payday lending whether inside or outside of the institution's assessment area should have their CRA performance more closely monitored without geographic limitations.

Predatory and Subprime Lending

Predatory lending is a harmful form of lending that can have a destabilizing effect on low and moderate-income neighborhoods as these lenders often target the most vulnerable segments of the population (low and moderate-income borrowers, elderly, minorities). Warning signs of a predatory loan include high interest rate (APR); high fees and closing costs; multiple refinancings (flipping); unnecessary debt consolidation; balloon payments; negative amortization; back-dating of loan documents;

large loan broker fees or kickbacks; loan based on property value/available equity rather than the borrower's ability to repay; "packing" of credit insurance or other products; and terms at closing different from what the borrower thought they would get. Predatory lending is also often accompanied by high pressure sales tactics or advertising. Subprime lending makes credit available to individuals who due to past credit problems or other circumstances do not qualify for conventional credit products or meet standard underwriting criteria. When conducted in a reasonable and responsible manner, subprime lending makes credit available to those who might not otherwise have access to credit. In recent years a number of institutions have chosen to engage in subprime lending activity by either originating subprime loans or purchasing investment vehicles secured by subprime loans. The Division believes that the CRA regulations should address an institution's participation in subprime lending activity. When conducted in a responsible and safe and sound manner, subprime lending can serve to increase available credit options for an institution's assessment area and receive CRA consideration. However, it is the Division's belief that an institution's participation in predatory lending activities, whether directly or indirectly should have a negative impact on the institution's CRA rating. Institutions should be held accountable for purchasing investment vehicles (e.g. mortgage-backed securities) secured by loans with unconscionable rates and terms and should be instructed to conduct due diligence in researching such investments for safety and soundness and compliance concerns. Institutions should also be held accountable for maintaining business relationships with entities that engaged in predatory lending activities. The Division believes that an institution's participation in predatory lending activities should be specifically addressed within the CRA regulation.

Assessment Area Designation for Internet Banks and Other Non-Traditional Entities

Currently, the CRA regulation does not contain any guidance for assessment area designation for Internet Banks or other non-traditional entities. With the increasing use of technology consumers are not required to go to a brick and mortar bank branch in order to conduct banking business. In addition, the Division notes that Federal bank agencies have issued charters to some entities (e.g. insurance companies) that operate on a national basis with non-traditional distribution networks. Because these types of entities are not limited to a specific geographic area it is difficult to apply current assessment area requirements to them. Under the current CRA regulations institutions must designate an assessment area based on certain geographic components (i.e.. Metropolitan Statistical Areas (MSAs); geographies in which the institution has its main office, branches, and deposit taking ATMs; and surrounding geographies in which the institution has originated or purchased a substantial portion of its loans). The regulations also provide guidance for wholesale and limited purpose institutions and institutions that serve military personal. Given that Internet Banks can generate deposits and/or originate loans from almost anywhere it is difficult to apply a geographic component to an evaluation of the institution's CRA performance. The Division notes that the CRA regulations stipulate that institutions serving military personnel who are not located within a defined geographic area may delineate their deposit customer base as their assessment area. The Massachusetts CRA regulation stipulates that a Massachusetts-chartered credit union whose membership by-law provisions are not based on residence may delineate its membership as its assessment area. The Division recommends that consideration be given to eliminating the geographic requirement for defining assessment areas for Internet Banks and other non-traditional entities that operate outside of the realm of regular geographic boundaries as such a requirement does not allow for an adequate or reasonable expectation for meeting credit needs within a specific geographic area.

Financial Literacy and Consumer Education Programs

Many financial institutions participate in financial literacy and consumer education programs within the communities that they serve. The Division notes the important role that financial literacy programs play in informing consumers about credit, budgeting, debt management and basic banking information. While financial institutions are encouraged to participate in these types of programs often times they find it difficult to receive CRA consideration for their participation. This is particularly true for institutions that may operate in areas without a significant low and moderate-income population. The Division has found that financial literacy and education programs can benefit all consumers. It is the Division's belief that the CRA regulations and Q & As should place greater focus on financial literacy and consumer education programs for all consumers and not just to those of low and moderate-income.

Purchased Loans

Currently under the Lending Test consideration is given both to loan originations and loan purchases. The Division believes that greater due diligence should be applied to purchased loans. In addition, the quality of the loans should be taken into consideration when evaluating the institution's CRA performance. Institutions should be held accountable for purchasing loans that may contain predatory terms or violate fair lending laws and regulations. Such accountability should be applied whether or not the purchased loans were originated inside or outside of the bank's assessment area.

Investments

The Investment Test portion of the CRA examination has been cause for much discussion. Some financial institutions have argued that the Investment Test should be eliminated or changed to count for "extra credit" in deriving an overall CRA rating. The Division believes that the proper evaluation of qualified investments is the alternative to elimination of the Investment Test. The Division believes that under the current regulations qualified investments are too narrowly defined. This has made it more difficult for institutions to receive CRA consideration for some of their investment activities. For example, under the current regulations it is extremely difficult for an institution that purchases municipal bonds from their local government to receive investment credit for this activity. Institutions that purchase municipal securities from local governments are helping to support economic development within that community and should receive CRA consideration for this activity. The regulation should allow for greater flexibility in the level of consideration given to investments. In addition, investments should be evaluated in three ways: 1) Current commitments; 2) Actual monies invested during the examination period; and 3) Fully funded investments that are still on the institution's books.

Community Development Activities of Large Retail Institutions

The Division believes that the current CRA regulations place too much emphasis on "double counting" between community development lending and HMDA-reportable and small business lending. During the course of our CRA examinations, the Division has come across numerous loans, which, although they meet a community development purpose, were unable to be considered under community development lending because they were HMDA-reportable or small business loans. Often times, these loans demonstrate an institution's commitment to meeting affordable housing or economic development

needs within the communities that they serve. The Division believes that the regulation should allow for greater flexibility in the level of consideration given to loans that may fit in more than one category.

The ANPR also discusses whether there is some merit in evaluating an institution's overall community development performance under one test. The Division notes that often times an institution's response to community development will be a strategy consisting of several different components (i.e. lending, investments and services) that work together. By evaluating community development under one test regulators could eliminate artificial distinctions in an institution's actual community development performance.

Acceptance of State CRA Examination Reports

As mentioned previously there are currently three states (Massachusetts, Connecticut and New York) that examine financial institutions for compliance with CRA on the state level. The Massachusetts CRA regulation is consistent with the federal CRA regulations. Further, the Massachusetts CRA regulations not only include the relevant federal provisions but in many respects they are more expansive. The Massachusetts CRA does not contain an exemption for special-purpose banks. In addition, the Massachusetts CRA is applied to uninsured branches of foreign banks as well as credit unions. The Division also continues to rely on the federal CRA examination procedures in all of our CRA examinations.

The Division notes that the Riegle-Neal Interstate Banking and Branching Efficiency Act of 1994 (Public Law 103-123) recognizes the applicability of state CRA laws while the Riegle Community Development and Regulatory Improvement Act of 1994 allows for the acceptance of state examination reports by federal banking agencies. The Division believes that an exemption from the requirements of the federal CRA regulations is not prohibited under federal law for those states that have parallel CRA requirements and the ability to enforce such provisions. The Division believes that the acceptance of its CRA examination reports would provide a direct regulatory relief to state-chartered banks, as they would not be subject to examinations more frequently than federally chartered banks. As such, the Division recommends that in the review of the current federal CRA regulations consideration be given to adding a provision specifying that federal banking agencies can accept CRA examination reports from those state banking agencies which have parallel CRA requirements.

Thank you for the opportunity to offer these comments. Should you have any questions please feel free to contact me at (617) 956-1500, extension 510 or Bonita Irving, Deputy Commissioner for CRA and Outreach at extension 561.

Very truly yours,

Thomas J. Curry
Commissioner of Banks