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CANICCOR
AN INTERFAITH COUNCIL ON CORPORATE ACCOUNTABILITY

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12 October 2001

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

Re: Docket No. 2001-49 - Community Reinvestment Act Regulations

The following comments arise out of the work of CANICCOR, which consists of:

- Serving as a consultant to institutional investors such as the Presbyterian Church (USA), the Evangelical Lutheran Church in America, Catholic Healthcare West, the Board of Pensions and Health Benefits of the United Methodist Church and Walden Asset Management. This work usually includes detailed reports based upon the HMDA and CRA data followed by dialogue with the financial institutions.

- Providing reports on financial institutions to screened funds as well as providers of such screening, such as KLD & Co. These reports are based upon the HMDA and CRA data as well as regulatory CRA Performance Evaluations.

1. Large Retail Institutions: Lending, Investment and Service Tests

The lending test is the most important test and the results of the performance test should constitute at least 50% of the performance grade. Thus, we support the present matrix requirement that a depository much achieve at least a low-satisfactory performance on the lending test to receive an overall satisfactory performance. However, CANICCOR supports a more quantitative approach, as outlined below.

A: Lending Test:

The lending test is essential to effectively assessing an institution's record of helping to meet the credit needs of its community. As noted below, certain changes would be helpful to increase the quantitative aspects of the test.

Detailed Quantitative Comparisons are Needed:

The performance should be measured quantitatively against a specified peer group of institutions or the industry as a whole, indicating how the proportion of loans to low-moderate income borrowers compares to the peer group. The lender should seek to lend to all borrowers equally, especially all low-moderate income borrowers, which is a group that tends to be underserved. In addition within the lending to low-moderate income borrowers, tests should be done to see if the lender is lending to specific minority borrowers proportional to the peer group or industry.

Development and Third Party Lending: See comments below under D.

Purchased Loans:

Several institutional investors, for whom CANICCOR served as consultant, were in dialogue several years ago with a large bank holding corporation concerning the need to improve their purchase loan performance. The corporation argued that they had a superior performance because their purchased purchase loans should be counted. They had a very large servicing platform with a large amount of servicing of FHA loans, which they wanted counted. We do not believe that these purchased loans from the servicing platform should be counted toward CRA goals of the affiliated depositories.

On the other hand, we have had dialogues with at least one major independent mortgage company that is able to make creative "CRA loans" because it then sells them to depositories. These sales are very useful in providing low-income and minority borrowers with loans and should be counted toward the CRA performance of the purchasing bank or thrift, so long as the purchaser intends to hold the loan as a portfolio investment.

As a result of these experiences, we suggest the following modification of 12 CFR__22(a)(2) to read:

The (agency) considers originations of loans and purchase loans, ***when the latter are purchased in the year of origination and are non-conforming, exclusive of jumbo loans, to be held as a portfolio investment. Non-conforming designates loans not capable of being sold to one of the Government Sponsored Enterprises: FNMA, FHLMC, GNMA or FmHA.***

Purchased loans that to not qualify under this proposed rule should not be counted for CRA purposes unless held as a portfolio investment, where they should be counted under the investment test in the same fashion as asset-backed securities but with higher priority.

The attached paper, *Position Statement on the Use of Purchased Loans for Community Reinvestment Act Purposes,* of May 1997 provides a detailed argument.

Loans with harmful or abusive terms:

Subprime and manufactured home loans can significantly improve the lending test performance. In our peer group analysis for institutional investors with screens, the unweighted performance for the 9 largest subprime lenders to low-moderate income borrowers was 28% above the total performance of all HMDA reporters in 1999 on purchase loans. For lending to African Americans the performance was 69% above the industry. By unweighted performance is meant the performance was based upon the number of loans to low-moderate income borrowers without additional weighting factors (see below).

We believe that subprime and manufactured housing loans fill an important niche for low-income and credit-impaired households. However, loans with harmful or abusive terms should be excluded. The question then becomes what are the criteria for exclusion. Obviously delinquency rates would be an ideal measure, but there must be some seasoning of the loans before this can be measured. Thus these delinquencies would not be able to be captured in the HMDA data.

Since the CRA Performance Evaluation of the depository, by its federal regulator covers at least a couple of years, the 90+day delinquency rate on subprime loans relative to conventional loans could be used to disqualify loans with APR's above some level such as 5% above long-term treasuries if this delinquency rate is above some value such as 4% above conventional delinquencies. However, the depository should then have the option to show that it has subsequently corrected the problem in the intervening time after the origination of these loans. (Note that delinquency rates are preferable to loans in foreclosure since the latter are often sold off to companies specializing in their workout.)

So far as the CANICCOR analysis for investors with screens is concerned, we would probably weight the loans inversely proportional to their APRs, assuming that the APR will be reported under the new regulations. The weighting could even become negative in the case of HOEPA loans, assuming they are also reported separately under HMDA. I should note that in order to account for small loans in a reasonable manner, CANICCOR now weights loans by the ratio of loan amount to the income of the borrower in our analysis of all owner-occupied single-family housing loans for institutional investors.

B. Investment Test:

There are very useful investments that a depository or its affiliates can make for community development of which investments in community development corporations are an example that should be highly rated. However, general purchase for portfolio-holding of loans, either individual or securitized, to low-moderate income borrowers and/or in low-moderate income tracts is useful in creating demand for the origination of these loans. This is the test for the broader range of these loans, not under the lending test.

C. Service Test:

The service test is a useful test but it needs to be more quantified. A quantified definition of service obviates the question of branches, etc. If an area has large numbers of depositors, both individual and small business, then the question of bricks and mortar is much less important since these customers may be using other modes of banking. This quantification should include:

a. The number of transaction accounts of individuals in low-moderate income and high minority tracts should be reported as well as those for small businesses. Geocoding programs are now very efficient so that the address of the account can easily be assigned to a census tract. These data should be made publicly available by census tract category and county along with the total number of such accounts in the CRA database.

b. From personal experience I have seen numerous people without accounts cashing checks at the bank I use. Here again, it would not be difficult to count these transactions and report them under CRA.

D. Community Development Activities:

a. Some geographic specification of development and third party loans as well as the purpose of each loan is essential to adequately evaluate these loans on a quantitative basis. The proof that innovative programs are of value is shown by the fact that people in low-moderate income and high minority areas are using these programs.

- The reporting of the number of loans and total amount at the county or MSA level would permit an evaluation of whether certain areas are receiving enough of such lending. Thus we should be able to look at an MSA and determine which lender is providing the major support for third party and development lending and which should provide more. This information would be very helpful in the case of large depositories such as those of the Bank of America or Wells Fargo because of their extensive assessment areas. These data should be made available with the CRA data as they are presently supplied.

- Multifamily housing loans can be double counted: once under multifamily originations and once under development loans. A notation as to the relative extent of this overlap would be useful, especially for savings institutions, which specialize in multifamily lending. Obviously, if each loan were reported with its purpose indicated, this problem would be obviated.

b. We also maintain that the large retail institutions as well as wholesale and limited purpose institutions should receive full consideration for community development activities anywhere they are conducted so long as the needs of their usually small assessment areas have been adequately addressed. See below for a further discussion under assessment areas.

c. These development activities should be considered under their respective tests: Lending, investment and service. We urge that the investment activities should also be reported under CRA as the development and third party loans are presently reported.

2. Small Institutions

In terms of the concerns of the investors, the $250 million and below definition of a small institution is reasonable so long as small banks, which are subsidiaries of large holding companies, are not included in the definition. At the present time a bank of any size is not considered a small institution if it is held by a holding company of $1 billion or more. We maintain that it would be useful to lower the limit of the bank holding company from the present $1 billion to $250 million. So far as the equity investor is concerned, it is the size of the bank holding company that is important, not how the assets may be distributed among subsidiaries. Thus the investor needs all the information provided under the CRA reporting of assessment areas, and small business lending for each of the subsidiaries of the total holding company.

3. Limited Purpose and Wholesale Institutions: The Community Development Test

See the comments under (6) Assessment Areas.

4. Strategic Plan

It is not the plan but the results of the plan that concern us. Thus the strategic plan must have concrete goals that are verifiable against standards of lending of the industry. It should be only used when a lender has novel features to its lending that it wants its regulator to certify as acceptable in principle.

5. Performance Contest

The question is where to draw the line between context and some absolute level of performance. In general, the broad categories of loans must be decided upon by the business plan of the depository and its affiliates. However, in our analysis for institutional investors, FHA and VA loans are always included in the industry reference for comparison with the institution's lending. Lenders, who do not provide FHA and VA loans, are expected to develop products that are serviceable to the same clientele as the FHA and VA loans. We maintain that savings institutions, which originate primarily adjustable rate mortgages, should not only be compared to other savings institutions but should be required to address the problem of reaching low-moderate income and minority borrowers though creative loan programs. They should be compared to the lending including fixed rate mortgages even though they make primarily adjustable rate mortgages.

6. Assessment Areas

The delineation of assessment areas is of vital concern to the CANICCOR analysis, particularly that of smaller institutions. The assessment areas provided with the CRA data permit us to evaluate smaller banks that operate in geographical areas less than the size of an MSA, which is our normal default performance area. Thus it is unfair to assume that a smaller institution in the New York MSA is also lending in Harlem when it only operates in Westchester County.

For larger institutions the present definition of assessment area is also useful because these are areas in which the depository has intimate knowledge of the market and where presumably most of their lending and that of their affiliates occurs. However, the use of other channels for acquiring deposits and originating loans which extent outside of the assessment area should also be considered in the CRA performance evaluation. An example is the very wide distribution of the small business loans by Wells Fargo Bank beyond its assessment areas. The proportion of these loans in low-moderate income tracts in the non-assessment areas should be a part of the performance evaluation

Finally, there is the recent spate of thrift charters to traditional non-depository finance companies. The lending of these affiliated non-depositories should be included in the CRA performance evaluation of the depository. This performance evaluation should include all of the affiliated non-depositories lending throughout the country. See also "Activities of Affiliates" for further development of this line of argument.

To solve this problem, we propose that:

A depository should have the totality of a given product line evaluated both within and outside of its assessment areas under the CRA performance evaluation, when more than 25% of the dollar amount of a given product line is provided to households outside of its assessment areas.

Obviously the percentage is arbitrary, but some percentage of 25% or less seems reasonable.

We agree that wholesale and special purpose depositories should be able to count loans and investments outside of their assessment areas as contributions to their CRA efforts.

7. Activities of Affiliates

We maintain that the lending of non-depository affiliated lenders of the depository should be required to be included in the CRA performance evaluation of the depository within its assessment areas. The need is especially true as the mortgage lending operations and subprime and manufactured housing lending operations are more and more segmented off into affiliated non-depository corporations.

Let us return to the discussion of large finance companies with small thrifts or banks as subsidiaries. The problem is that these depositories are primarily useful in the payments system and are not making loans of the type provided by the affiliated finance company. However, we maintain that the total lending of the affiliated finance company should be a part of the CRA performance evaluation and that assessment area definitions are irrelevant. Thus we suggest that:

Depositories, which serve substantially as part of the payments system or as a capital source for an affiliated non-depository lender, should have all the lending of the affiliated lenders included in their CRA performance evaluations.

Equally important is the lending by large mortgage subsidiaries of a corporation. These mortgage companies may only be indirectly affiliated with one or more of the depository subsidiaries through the parent corporation. Their lending in the assessment areas of the depositories is easily captured and should be counted in the performance evaluation of the depository. ***If more than 25% of the lending of such a mortgage company is not accounted*** **for in the assessment areas of the several depository subsidiaries, the remainder of the lending should be parsed among the depository subsidiaries geographically based upon depository asset size.**

8. Data Collection and Maintenance of Public Files

Small Business Loans:

The data on small business loans, as they are now reported, are not very useful. CANICCOR would prefer more information on each loan with less geographic specificity. Thus we would prefer reporting within a county or an MSA of individual loans with loan amounts, the annual turnover of the borrower, and a broad geographic category, such as just the three tract income categories: low-moderate, middle and upper. Possibly, the APR should also be included to indicate subprime and credit card lending. The loan amounts are useful especially to screen out credit card loans, and the annual turnover or sales of the borrower is crucial in the same fashion as the income of the borrower is for housing loans. It would also be helpful to know if a loan is real estate related, although this can generally be guessed from the ratio of the loan amount to annual turnover.

Other Data Issues that have already been discussed include:

Need to report:

Development and third-party loans by county and
APR of loans to provide an indication of which loans are subprime loans.

Acknowledgement

CANICCOR appreciates this opportunity of providing comments on this advance notice of proposed rulemaking. The revisions of 1995 were significant improvements to the CRA regulations, and it is important that the vagaries and omissions of those rules be addressed while maintaining the advances made at that time.

Sincerely yours,

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