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January 21, 2005

Filed via email to regs.comments@ots.treas.gov

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

Re: No. 2004-53; 12 CFR Part 563e; Community Reinvestment Act - Community Development, Assigned Ratings; 69 Federal Register 68257; November 24, 2004

Dear Sir or Madam:

The Office of Thrift Supervision (OTS) is proposing two significant changes to the OTS regulations implementing the Community Reinvestment Act (CRA). First, the OTS proposes to amend the definition of "community development" to encourage more community development activities by large savings associations in nonmetropolitan areas and in areas subject to natural and other disasters and other community-wide disruptions. Second, the OTS proposes to revise how it assigns its CRA ratings by allowing large savings associations to self-determine what weight each of the three tests (lending, service, and investment) will contribute to the overall CRA performance rating. These changes will positively affect all savings associations in varying degrees, and the American Bankers Association supports the proposed changes. The American Bankers Association (ABA) brings together all categories of banking institutions to best represent the interests of this rapidly changing industry. Its membership - which includes community, regional and money center banks and holding companies, as well as savings associations, trust companies and savings banks - makes ABA the largest banking trade association in the country.

Proposed Changes to the Definition of Community Development

1. Proposal that "Community Development" Include Rural Residents

The OTS proposes to change the definition of "community development" from only focusing on low- and moderate-income area residents to including rural residents. The OTS states that this proposed change is intended to allow a broader range of activities by banks in rural areas to receive CRA credit. **The ABA strongly supports the OTS's proposal.**

ABA and OTS are both aware that the CRA definition of “community development” has a strongly urban focus. As a result, there are often very few opportunities for savings associations with rural areas in their assessment areas to provide qualified CRA loans, investments or services, as evidenced by the example provided in the sidebar. In that example, the institution was required to make “regional” investments that are highly unlikely to be returned to the institution’s community. It is our members’ experience that the investment test forces disinvestment from largely rural areas. Under the proposed expanded definition, community development would also include: (1) community services targeted to individuals in rural areas; and (2) activities that revitalize or stabilize rural areas. Community development activities in rural areas would be covered even if the individuals or areas served are not low- or moderate-income.

From a 2004 OTS CRA Public Evaluation of a \$1.5 billion savings association:
 “While community development opportunities may exist, the rural nature of most of [the institution’s] assessment areas makes such opportunities difficult to find.”
 Among other investments, the institution committed over \$2 million in regional investments that “included” the largely rural assessment area.

The OTS proposal is essentially identical to a pending Federal Deposit Insurance Corporation’s (FDIC) proposal that ABA also strongly supports. We support these proposals because, in reviewing the CRA Performance Evaluations of rural banks and savings associations, one so often finds examination findings that read: “[g]iven the limited opportunities for the bank to purchase qualifying community development debt or equity investments in its assessment area, the level is considered acceptable.” We suspect this is now a standard paragraph for examiners. ABA concludes that rural communities are being short-changed by the current regulatory definition of “community development” under CRA.

Therefore, ABA believes that the enlargement of the definition of “community development” to include rural residents, even if the census tract (which may contain tens or even hundreds of square miles in largely rural areas) is not an LMI census tract, would go a long way toward eliminating the current distortions in the regulations. These distortions can and do result in a largely rural or small community institution being told to invest in housing bonds in statewide areas that will probably never benefit the institution’s community, as shown in the sidebar to this paragraph. The OTS’s proposal would lessen the occurrence of such anomalies. The OTS also asks whether the regulation should authorize the Director of OTS to determine that additional activities that benefit the public welfare also constitute “community development.” ABA supports the adoption of this provision to provide an on-going mechanism for ensuring that “community development” activities continue to be focused on the institution’s assessment area(s).

In a 2003 OTS CRA Public Evaluation of a \$1.5 billion savings association, the association received a High Satisfactory for its lending and a High Satisfactory on its service, but received a Low Satisfactory on its investments, dragging down the institution’s CRA rating. Because of the low level of suitable investments in the institution’s community, it bought a single large mortgage backed security, for loans to LMI borrowers or for loans secured by property located in LMI geographies throughout the state.

ABA strongly supports enlarging the definition of “community development” to include specifically rural residents, irrespective of the median income of their census tract.

The OTS further asks if “rural” needs to be defined, and if so, how that term should be defined. ABA notes, as ABA commented to the FDIC on its proposal, that some CRA activists have already suggested that the OTS’s proposal would allow CRA credit for loans to upper-income, part-time hobby farmers or to “farming” communities in affluent suburbs. First, we note that the present definition of “community development” already includes loans to small farms, if they meet the size eligibility standards of the Small Business Administration, irrespective of the income of the owners, so that changing the definition will not affect the validity of those loans. However, there are more than farmers who are rural residents needing credit, and we, as noted above, do support enlarging the definition of community development to include those rural residents who are not owners of farms. In that case, it appears to ABA that a clear definition of “rural” would assist both bankers and examiners in determining whether a loan qualifies for consideration as a “community development” loan. Therefore, ABA urges the OTS to explore the possibility of better defining the term “rural” in order to provide clear guidance to bankers and examiners.

ABA has looked at several possible definitions of “rural,” and we tentatively favor use of “metro” and “non-metro counties,” as designated by the Office of Management and the Budget. In 2003, OMB defined metro areas as (1) central counties with one or more urbanized areas, and (2) outlying counties that are economically tied to the core counties as measured by work commuting. Outlying counties are included if 25 percent of workers living in the county commute to the central counties, or if 25 percent of the employment in the county consists of workers coming out from the central counties—the so-called “reverse” commuting pattern. Non-metro counties are outside the boundaries of metro areas and are further subdivided into two types: micropolitan areas centered on urban clusters of 10,000 or more persons and all remaining “noncore” counties. The advantage to this definition is that it generally reflects the political subdivisions of the state and are readily understandable.

However, the disadvantage of the use of metro/non-metro is that it appears to us to allow suburban sprawl around urban centers to overwhelm rural populations, leaving the rural residents without the opportunity to benefit from the proposed change in the definition of community development. ABA has already heard from three agricultural banks that are now Home Mortgage Disclosure Act reporters because their rural counties are on the edge of major urban sprawl and were reclassified as part of an MSA, even though the banks are on the other side of the county. Thus, it appears that the metro/non-metro approach does not cover all rural residents and that there will need to be an alternate test for rural that will not exclude those rural residents whose counties are on the edges of major metropolitan centers. ABA regulatory and agricultural lending staff members are available to work with the OTS staff to achieve an appropriately flexible definition of “rural.”

2. Proposal That Community Development Include Various Disaster Areas

The OTS also solicits comment on further encouraging savings associations to perform community development activities in any areas affected by natural or other disasters or other major community disruptions, such as areas of Florida devastated by hurricanes last year. This portion of the proposal would not be limited to rural areas or activities targeted to low- or moderate-income individuals or low- or moderate-income geographies. ABA believes this change to be appropriate and consistent with the statutory language of the Community Reinvestment Act that requires the agencies to “assess the institution’s record of meeting the credit needs of its entire community, including low- and moderate-income neighborhoods, consistent with the safe and sound operation of such institution.” [Emphasis added.]

ABA also supports this proposed change to define community development activities in disaster areas or areas of other major community disruption as qualified community development activities under CRA.

Proposed Changes to How CRA Ratings are Assigned

Currently, large retail institutions are evaluated on a matrix of scores on three tests: lending, service, and investment. Lending has a weight of 50% of the total score, while service and investments have weightings of 25% each. OTS is proposing to allow each savings association evaluated under the large retail institution test a choice, at its option, on the weight given to lending, investment, and service in assessing its CRA performance. OTS would not allow less than a 50 percent weight to lending. The remaining 50% would weigh lending, investment, or service, or some combination thereof, based on the savings association's election. As a result, each savings association could choose to have OTS weigh lending anywhere from 50% to 100% for that association's overall performance assessment, services anywhere from 0% to 50%, and investments anywhere from 0% to 50%. In effect, the proposal would allow large savings associations to focus on lending and service and to not have their investment considered for their CRA rating. In the alternative, the OTS asks whether it should just eliminate the investment test.

ABA has opposed the investment test since it was first proposed over a decade ago. As we said then and have said consistently thereafter, the primary focus of the Community Reinvestment Act is the requirement that the Agencies evaluate insured depository institutions on their record of helping to meet the credit needs of the entire community. ABA believes that the creation of the mandatory investment test in 1995 shifted the focus too much away from the provision of credit and placed too much emphasis on community development and investment. In fact, the current regulations in too many instances actually result in requiring institutions to send money OUT of their communities, as indicated by the sidebar to this paragraph.

In a 2003 OTS CRA Public Evaluation of an over \$10 billion savings association, OTS gave the institution an Outstanding rating, based in part on its high level of qualifying investments. However, as noted in the examination "[t]he investments benefit the assessment areas as well as broader statewide areas." That is, the majority of the investment was outside of the institution's assessment area.

Instead ABA has recommended that the investment test be eliminated, but that investments should be substitutable for loans. The OTS proposal effectively allows a large institution to choose that approach to CRA while still allowing large institutions with major community development and investment programs to continue to have those investments count towards their CRA rating. Therefore, ABA supports the OTS proposal. Additionally, as part of the proposal, OTS asks several related questions.

OTS asks if it would be appropriate to provide the savings association flexibility in the way that CRA ratings are assigned by offering a choice of weights for the lending, service, and investment tests? ABA does not see the need for providing such pre-set choices, as it appears to reduce the flexibility at the OTS is seeking to increase by its proposal.

OTS further asks what the impact would be on lending, investments, and services of offering alternative weights? ABA concludes that alternative weights would only increase the importance of lending, given that the OTS proposal never allows lending to be less than 50% in weight. Since CRA is simply about helping to meet the credit needs of the entire community, the impact of the OTS's proposal would appear to be to increase the provision of credit to the community, which is exactly what CRA requires the Agencies to do.

OTS also asks if it would be appropriate to provide an alternative that would allow the weighting of lending at less than 50%? ABA does not support such an alternative, as it would be inconsistent with the Community Reinvestment Act. The regulations already provide for limited purpose or wholesale institutions with a limited ability to retail lend to apply for the limited purpose or wholesale institution examination or to opt for the strategic plan. ABA believes that those options provide sufficient flexibility to make unnecessary the weighting of lending below 50% in the regular large institution examination.

OTS asks if a rating matrix that allowed a savings association to receive a rating of “satisfactory” without receiving at least “low satisfactory” on the lending test were offered, would that be consistent with the purposes of CRA? Consistent with ABA’s emphasis on returning to the core of the CRA statute, which is the institution’s record of helping to meet the credit needs of the entire community, ABA supports requiring that, to receive a “satisfactory” rating, an institution must be at least a “low satisfactory” in lending.

Finally, OTS asks if it would be preferable to eliminate the investment test? The OTS proposal adds to the flexibility of CRA by allowing institutions with established investment test programs to continue to do their good work while allowing institutions that wish to focus on lending in their communities to do so. For example, an institution that is doing well in providing services and credit to its community should not be required to make any investments, as it has already met the credit needs of its community. Under the proposal, it then could opt to have the lending test count for 75% of its grade and the service test for 25% of its grade and the investment test would be effectively eliminated for this institution. However, those large savings associations that have extensive community development programs and have Outstanding investment test ratings will continue to include their investments in an investment test. **For all of these reasons, ABA strongly supports the OTS’s proposal to revise the way CRA ratings are assigned.**

Conclusion

ABA commends the OTS for the bold new approach to revising the CRA regulations. ABA supports the proposed changes in the definition of community development for all savings associations to better recognize the provision of credit to rural residents and to include community development in disaster areas. Finally, ABA strongly supports the OTS’s proposal to revise the CRA ratings system, which ABA believes will return the focus of CRA to the provision of credit to the entire community, where the Community Reinvestment Act statute states that it should be. If the OTS has any questions about this comment letter, please call the undersigned.

Sincerely,



Paul Smith
Senior Counsel