NATIONAL MERCANTILE BANCORP

January 21, 2005

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

Office of Comptroller of the Currency
Communications Division
Washington, DC 20219

RE: OTS Community Reinvestment Act Proposal

Ladies and Gentlemen:

The enclosed letter from CBA to OTS regarding the OTS' proposal permitting institutions to align their community reinvestment activities in accordance with their business focus and their experience and expertise has the full agreement and support of National Mercantile Bank and encourage its adoption.

National Mercantile Bancorp, a bank holding company with assets of less than Five Hundred Million Dollars ($500MM), does not have the excess personnel and supporting infrastructure to conduct the necessary due diligence needed to identify and evaluate investment opportunities that are suitable for CRA purposes as well as for the Bank.

Your positive consideration to the OTS' proposal is greatly appreciated.

Sincerely,

Tom Aita
Senior Vice President
(Acting) CRA Officer

Scott Montgomery
President

Enclosure:

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

Re: OTS Community Reinvestment Act Proposal

Ladies and Gentlemen:

The California Bankers Association ("CBA") appreciates this opportunity to provide comments to the OTS' proposed rulemaking regarding the Community Reinvestment Act "Proposal"). CBA is a professional nonprofit organization established in 1891 representing virtually all of the depository financial institutions in California, including most of the savings institutions in the state. CBA strongly supports the proposal to permit large financial institutions to determine the relative weights to be applied to the three CRA sub-tests in deriving the overall CRA rating.

Proposal consistent with CRA

The Proposal is entirely consistent with the text and congressional purpose of the Community Reinvestment Act, which is to encourage depository financial institutions to help meet the *credit* needs of the local communities in which they are chartered. (12 U.S.C. 2901). We believe the Proposal, which permits institutions to align their community reinvestment activities in accordance with their business focus and their experience and expertise is also consistent with, and is an extension of, applying performance context. Furthermore, this goal is achieved without eliminating investment and service activities.

Nowhere in the statute is there authority for the federal banking agencies to prescribe regulations related to investments and services. These subtests were created by regulation, and we believe the agencies exceeded their statutory authority in creating them. While there arguably exists a need to tailor CRA requirements to certain, non-traditional institutions that may not provide the type of lending contemplated under the law, we do not believe it is appropriate to impose industry-wide any requirements other than those permitted by the statute.

The irony is that these exceptions created to accommodate special-purpose institutions became the rule for all institutions, even if many institutions have no particular expertise in, for example, investments. Thus, a federal savings association, which typically places

a great emphasis on mortgage lending, is currently permitted to count only 50% of its lending toward its CRA rating. This is a distorted result and one that forces institutions to engage in activities that are inconsistent with their business focus and even their expertise.

Imposition of sub-tests burdensome for many institutions. The substantial majority of depository financial institutions engage primarily in lending activities. Outside of CRA requirements, many conduct investment activities only to the extent of managing assets and liabilities as necessary to balance lending and liquidity. Because of the fairly rigid 3-part CRA sub-test scheme now in effect, many banks are compelled to seek out investment opportunities that have little or no relation to the bank's business model.

The need to venture out to identify and evaluate investment opportunities that are suitable for CRA purposes is a time-consuming process. Many banks do not have the personnel and supporting infrastructure already in place to conduct the necessary due diligence to perform these functions. For example, a CBA member has related that, after searching unsuccessfully for investment opportunities, the bank finally settled on purchasing mortgage-backed securities because of the obvious connection to mortgage lending. But even then, the bank had to acquire knowledge about the risks of such investments and how to vet them. For medium-sized institutions in the one-to-several billion dollar asset-size category, these challenges are exacerbated by competition from the major institutions that have far greater resources and therefore have greater success in making the most suitable investments.

The result is that for too many banks, investments are sought out and made purely to satisfy regulatory requirements, and it is uncertain whether such activities necessarily benefit communities more than straight lending would. Under the proposal, financial institutions would have the flexibility to focus more on those activities that are more aligned with their expertise and resources.

On the other hand, the Proposal is ideal because if an institution has successfully made CRA investments and those investments have benefited communities in the manner contemplated under the statute, then those institutions would be permitted to continue to make them and earn credit for them. CBA also supports maintaining a minimum 50% weight given to lending as, again, credit is the central tenet of the statute.

Finally, CBA agrees that the Proposal is more consistent with the "performance context" approach in that institutions would not be subject to evaluation under the fairly strict 50-25-25 rule now in place. If the performance factors currently applied in the regulation suggest a different ratio or balance among the three tests, then an institution would be free to adjust its activities accordingly.

Deference to institution. How much deference the OTS should give to an institution's determination is an important policy consideration. First, as discussed above, any limits should be based on the overall purpose of the statute. Thus, as long as an institution is meeting the credit needs of the communities it serves, there should be no basis for a

material criticism of an institution's election. On the other hand, the OTS in its capacity of regulator should retain a degree of discretion to challenge an institution whose activities it deems to undermine the purpose of CRA. While CBA is not in a position to identify with specificity the circumstances in which an institution may be challenged, we note that the OTS currently gives deference to institutions in determining their performance context.

Elimination of investment test. The OTS also asks whether the investment test should be eliminated in its entirety. While CBA believes there is no statutory basis for the investment test, investment activities nevertheless have been part of CRA for a number of years, and have produced many positive outcomes. As long as the OTS adopts a rule that permits institutions to determine their own weighting, and such determination is accorded deference, CBA does not perceive the need to eliminate the investment test. Indeed, preservation of the investment test (under the conditions articulated) would encourage those institutions that have made successful investments to continue to do so.

Community development. CBA also supports liberalization of the concept of "community development" as applied to rural areas. We agree that lending and investment opportunities in rural areas that are qualified for CRA consideration can be limited, and in such circumstances, a financial institution can be left with few options on complying. We support the proposed clarification as a means of relieving this burden, that is, such activities that benefit persons and areas in rural locations can be qualifying even as to non-low- and moderate-income persons or areas.

CBA appreciates this opportunity to submit this letter on the OTS Proposal. The Proposal would give financial institutions needed flexibility in complying with the CRA, and yet remain consistent with the statute's purpose. For these reasons, CBA strongly supports the Proposal. If you have any questions for comments, please feel free to contact the undersigned.

Sincerely,

Leland Chan
General Counsel