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Re: **FDIC** - 12 CFR Part 345 - RIN 3064–AC89; **FRB** - Docket No. R-1225; **OCC** - Docket No. 05–04; Proposed Revisions to the Community Reinvestment Act Regulations; 70 Federal Register 12148; March 11, 2005

Dear Sir or Madam:

The Federal Deposit Insurance Corporation, the Board of Governors of the Federal Reserve Board, and the Office of the Comptroller of the Currency (the Agencies) have proposed amendments to the Community Reinvestment Act (CRA) regulations. The proposal would directly affect a few less than 1400 banks between $250 million and $1 billion in assets and would indirectly affect about 800 bank holding companies that hold one of the affected banks. ABA appreciates the opportunity to comment on this important proposal. The American Bankers Association, on behalf of the more than two million men and women who work in the nation's banks, 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.

The Agencies propose to (1) amend the definition of "small institution" to mean an institution with total assets of less than $1 billion, without regard to any holding company assets, and to index both the small and intermediate small bank thresholds on the basis of the Consumer Price Index; (2) add a new community development test (CD test) that would be separately rated in CRA examinations for banks between $250 million and $1 billion in assets (intermediate small banks); (3) expand the definition of "community development" to include: (a) affordable housing for individuals in underserved rural areas and designated disaster areas (in addition to low- or moderate-income (LMI) individuals) and (b) community development activities that revitalize or stabilize underserved rural areas and designated disaster areas (in addition to LMI areas); and (4) provide that evidence that an institution, or any of an institution's affiliates, the loans of which have been considered pursuant to §__.22(c), has engaged in specified discriminatory, illegal, or abusive credit practices in connection with certain loans would adversely affect the CRA rating.

<u>1. Raising the threshold of "small bank."</u> **ABA strongly supports raising the threshold of a "small bank" under CRA to $1 billion, without regard to the size of the holding company. ABA also supports indexing the size thresholds for both the small bank and the intermediate small bank annually, based on the Consumer Price Index**. Under the CRA regulations, the small bank examination imposes considerably less regulatory burden than does the large bank examination. With the increase in consolidation at the large end of the asset size spectrum, the gap in assets between the smallest and largest institutions has grown substantially since the line was drawn at $250 million in 1995. The growing asset gap between the smallest above-the-threshold institutions and the largest institutions has meant that the disproportion in compliance burden has grown on average heavier on smaller banks. ABA believes relieving the burden on small banks is vital to ensure their survival. Since 1995, the regulatory burden on small banks has grown significantly larger, including just in the last few years massive new reporting requirements under HMDA, the USA Patriot Act and the privacy provisions of the Gramm-Leach-Bliley Act. But the nature of community banks has not changed. When a community bank must comply with the requirements of the large institution CRA examination, the costs to and burdens on that community bank increase dramatically. This imposes a dramatically higher regulatory burden that drains both money and personnel away from actually helping to meet the credit needs of the institution's community. As a result, a bank with more than $250 million in assets but less than $1 billion faces significantly more requirements that substantially increase regulatory burdens without consistently producing additional benefits as contemplated by the Community Reinvestment Act.

Further, the number of institutions defined as small has declined by over 2,000 since the threshold was set in 1995, and the percentage of industry assets held by small banks has declined substantially. In fact, the percent of industry assets subject to the small bank examination at the beginning of 1996 was 14%. Raising the threshold today to $500 million only makes 11% of the industry's assets subject to the small bank examination. Raising the threshold to $1 billion makes 14% of industry assets subject to the small bank examination, **the same percentage of industry assets that were originally subject to the small bank exam.** Thus, if the proposal is adopted, 86% of industry assets would continue to be subject to the large bank examination as was the effect of the current regulation when it was adopted.

However, ABA concludes that this proposal does not actually increase the threshold for a small bank but rather creates a new class of bank: the intermediate small bank – one between $250 million and $1 billion – subject to a new and more burdensome examination than are small banks. Thus, for banks between $250 million and $500 million, the proposal offers considerably less relief from regulatory burden than the Agencies originally proposed on April 6, 2004 - to raise the small bank threshold to $500 million. The current small bank test imposes considerably less burden on a community bank than does the large bank test. ABA also concludes that it imposes considerably less burden than will the new intermediate small bank test. ABA believes that the Agencies were correct in their original proposal that the small bank examination does accurately capture the information necessary for examiners to assess whether that community bank is helping to meet the credit needs of its community. **ABA recommends that the threshold for a small bank subject to the existing small bank streamlined examination should be raised to at least $500 million.**

The streamlined examination for small banks actually does what the Community Reinvestment Act required of the Agencies: it requires examiners, during their examination of the bank, to look at the bank's loans and assess whether the bank is helping to meet the credit needs of the bank's entire community. It imposes no investment requirement on small banks, since the Act is about credit, not investment.[1] It adds no data reporting requirements on small banks, fulfilling the promise of the Act's sponsor, Senator Proxmire, that there would be no additional paperwork or recordkeeping burden imposed on banks if the Act passed. And it creates a simple, understandable assessment test of the bank's record of providing credit in its community: the test considers the institution's loan-to-deposit ratio; the percentage of loans in its assessment areas; its record of lending to borrowers of different income levels, including low- and moderate income borrowers, and businesses and farms of different sizes; the geographic distribution of its loans; and its record of taking action, if warranted, in response to written complaints about its performance in helping to meet credit needs in its assessment areas. This is a totally appropriate CRA evaluation for a community bank. And it needs to be applied at least to community banks up to $500 million.

An additional reason to raise the $250 million small bank threshold is to adjust for inflation. The Agencies now propose to include a CPI index adjustment for the threshold for small banks and for intermediate small banks. ABA thinks that if the Agencies believe that CPI indexing is a good idea now, then it should have been adopted when the original small bank threshold was created in 1995. After all, this proposal is part of the Agencies' promised review to determine if the 1995 revision

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[1] ABA believes it important to note that the streamlined small institution evaluation comes closest to what the Congress intended when adopting the Community Reinvestment Act. The Act itself provides that:
"SEC. 804. (a) IN GENERAL.--In connection with its examination of a financial institution, the appropriate Federal financial supervisory agency shall--
(1) 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;"

Since in 1977 there was only one examination of a financial institution, the safety and soundness examination, it is clear from the statute that the Agencies were to make a general assessment of the institution during that safety and soundness exam. No additional data collection, no additional paperwork and no service and investment tests were contemplated by Congress when it enacted the Community Reinvestment Act.

of the CRA regulations was working. For small banks, we know it is not, partly because the small bank threshold remains too low. If the Agencies just adjust the threshold for a small bank as a result of inflation from the end of 1995 to the end of 2004, the Agencies would have to raise the threshold of a small bank to **$310 million**. However, the percent of industry assets held by small banks has shrunk so much that the Agencies should raise the threshold at least to $500 million.

2. Intermediate small bank examination with separate CD test. The Agencies' proposed "intermediate small bank" test offers nowhere near the level of regulatory burden relief of their being defined as small banks under the current regulation, while it poses all of the uncertainties of learning a new examination with a separate community development test.[2] However, for banks between $500 million and $1 billion, the proposal holds out the certainty of relief from the CRA data collection and the possibility of a more flexible assessment of community development lending, services and investments than is provided in the current large bank test. One thing is certain for all of banks between $250 million and $1 billion, this proposal appears to be better than being a large bank. ABA knows this because we sent a letter to every bank in this size range asking whether this proposal was better than making no change, and the responses were almost unanimous that large bank test has been a regulatory nightmare. Overall, our banks support the proposal as better than doing nothing. For banks with assets of $500 million but less than $1 billion, the intermediate small bank test does present potential relief from the large bank test. Since banks can always opt to be considered as large banks, these larger banks will be able to choose between the lesser of two evils, as they gain experience with the intermediate small bank test.[3]

Our bankers believe that they support their communities and do community development lending, even if it is not recognized by the current regulations (see "Expanding the definition of community development" below). However, they do it as part of their overall provision of credit to their communities, and they believe it needs to be a part of the overall assessment of their records of helping to meet the credit needs of their communities, and **not** a special, separate test that can cause them to fail their CRA examination by itself. This approach appears to allow a bank to better tailor its community development activities to the bank's own strengths and to the bank's specific community, compared to the current separate consideration of CD lending, service and investment under the large bank test. **ABA supports an intermediate small bank examination for banks under $1 billion.**[4]

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[2] As one community banker said recently at a meeting on the proposal, "Only in Washington could someone create a whole new examination with several major undefined standards and call it regulatory burden reduction."

[3] ABA has been told by ten banks between $500 million and $1 billion that they will likely opt to be examined as large banks, since they already have their CRA compliance and reporting systems in place as large banks and they have Satisfactory or Outstanding ratings. Most of these are in multi-bank holding companies, and the cost of change appears to be considerably higher than any perceived possible benefit of moving to the "intermediate" examination.

[4] In fact, the community development test concept originated with very large banks. These banks believe that the rigid lending, service and investment tests for large banks make it more difficult for them to facilitate major community development projects. ABA urges the Agencies to evaluate how the CD test works and to extend it to large banks.

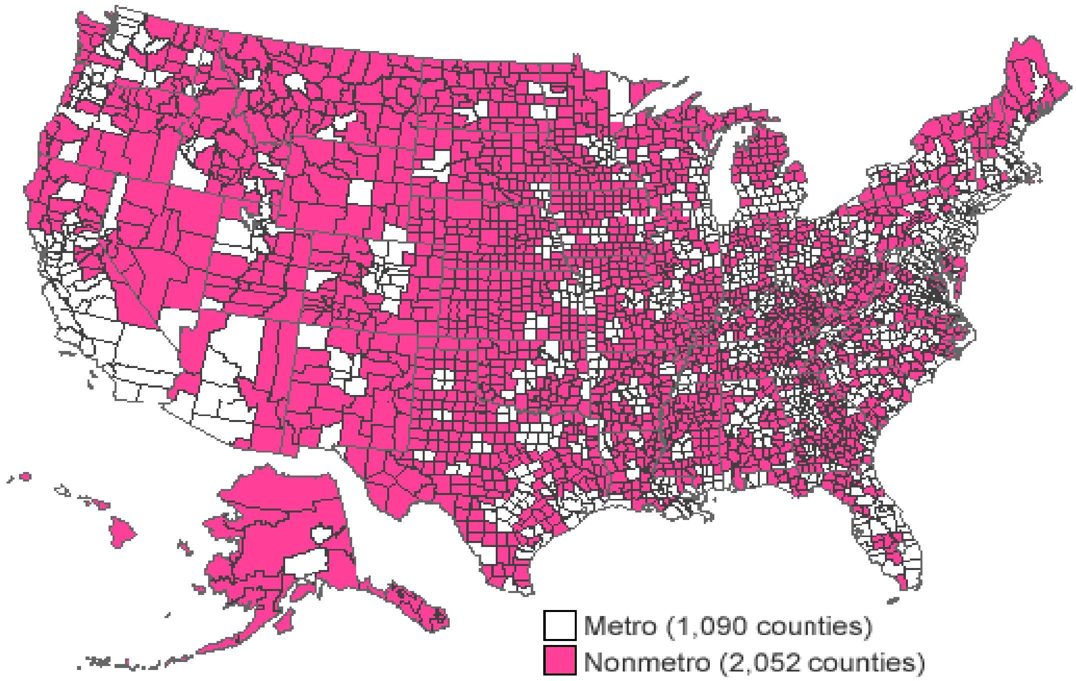
There is considerable support for the Agencies' proposed elimination of the large bank investment test and replacing it with a Community Development test that would look at the bank's CD lending, services and investments together. However, the CD test is being added as a **separate test** that must be passed in addition to an assessment of the bank's lending to its community. The result is a CD test that must be met with at least a Satisfactory rating, no matter how OUTSTANDING the bank's record of meeting the credit needs of its community. Not even the large bank's Investment Test has been granted this level of importance. Given that the term "community development" does not even appear in the Community Reinvestment Act itself, the elevation of "community development" to equal status with actually helping to meet the credit needs of the community (the essential requirement of the statute) is incomprehensible. Overall our banks oppose making the combined CD lending, services and investments test separate but equal in importance to providing credit to their communities. No reading of the Community Reinvestment Act itself can justify such a regulatory result. **ABA opposes a separate Community Development test.**

3. Expanding the definition of "community development." It is the experience of our rural banks that the current definition of "community development" shortchanges rural America. Too many of them have had to make contributions, investments or loans OUTSIDE of their communities in order to satisfy the large bank CRA test. Examples of this perverse result of the CRA regulations abound in the CRA Public Evaluations of large banks under $1 billion.[5] The regulations need to reverse this discrimination against rural areas. The Agencies have finally recognized that this part of the CRA regulations needs to be revised, and they propose to expand the definition of community development to include rural underserved areas. **ABA supports enlarging the definition of "community development" to stop the disinvestment in rural America caused by the present CRA regulations.**

We believe that any definition of rural should be easy to understand, easy to find, and relatively stable. One definition that appears to fit these criteria is the OMB's designation of "nonmetropolitan counties," as seen in the chart below. **ABA recommends that the Agencies define "rural" as those counties designated "nonmetropolitan" by the Office of Management and Budget.**

[5] A May 2002 CRA PE by the FDIC of a $500 million bank showed over $300,000 invested in a fund of which **none of the actual properties in the fund were located in the bank's assessment area**. A February 2003 CRA PE by the FDIC in which the examiners urged the bank to make investments out of its assessment area, since "[g]iven the limited opportunities locally, the Bank could expand its search for qualified investments on a broader basis…." We can provide many more examples.

Nonmetropolitan and metropolitan counties, 2003



Source: Prepared by ERS using data from the Census Bureau.

While our rural bankers are largely in agreement with this recommendation, there are a number of them that point out that, as a result of the growth of urban sprawl, many rural counties under the 1990 census that were adjacent to metropolitan areas were designated "metropolitan" counties by OMB under the 2000 census. This results in excluding large rural areas near urban centers from being designated as being in nonmetropolitan counties. As the rural community banks in those counties tell us, they are still serving their largely rural customer base, but they will not be allowed the benefit of the "rural" designation under CRA. **Thus ABA recommends that the Agencies allow banks that have largely rural assessment areas but are in metropolitan counties to work with their primary regulator to define which parts of their assessment areas are in fact rural, which regulator-approved designation would also meet the requirements of the CRA regulations for "rural."**

In addition to being rural, however, the Agencies also will require that the area for community development be "underserved." ABA does not want the definition of "underserved" to be so restrictive as to continue to push CRA investment out of rural areas, either from being so narrow that too few rural residents or areas qualify or from requiring so much documentation that it remains unworkable for most community banks. Under the current CRA regulations, many rural areas have few LMI tracts, partly because rural census tracts are generally larger and more economically heterogeneous than most urban tracts, since census tracts are defined to have a roughly equal number of people in them. This results in many rural LMI residents not being considered to be living in LMI areas.[6] To adjust, the Agencies propose using a different definition of LMI for rural tracts than urban tracts. Economists at the Federal Reserve Board have worked on various definitional changes and have presented a number of alternatives to industry trade associations and community development advocates and groups. Each approach has "winners and losers" in a particular rural area, as each approach results in slightly different demarcations of LMI tracts in rural areas. ABA does not recommend a specific approach, but ABA does support achieving a rough parity in LMI tracts in urban and rural areas. **ABA supports this proposal and recommends that the new definition of "underserved" include a definition of LMI for rural counties that would raise the number of LMI tracts in rural areas to a level that will ensure rough parity to the number of LMI census tracts in urban areas.**

While such a change will decrease the disparity between LMI areas in rural parts of the country versus urban parts, nonetheless ABA does not believe that by itself this change is sufficient. There will still be the problem that rural census tracts are larger and the LMI population is more dispersed than in urban areas. Thus, ABA concludes that a simple definition of a rural area as LMI does not sufficiently define "underserved." The Agencies ask for alternatives to changing the definition of LMI for defining "underserved." One would be to use the Community Development Financial Institutions Fund definition of underserved. Just using that definition would be a mistake: it changes every year and every examiner and every rural banker would have to keep a database of the annual definitions and where and when each loan was made to determine if a loan or investment qualified. However, if the CDFI definition was in addition to the change in the LMI definition, then community banks could reach out to areas that were not classified as LMI but which were underserved under the CDFI definitions. The CDFI definitions look to whether there has been a significant increase in unemployment or whether the location has a high poverty rate or a certain percentage of population loss, all of which conditions may be present in many rural communities. Agency staff also asks whether just using as a definition of "underserved" any area designated by a governmental agency for development. While this too would add areas not included under the other definitions, by itself ABA believes that it would be inadequate. To better address the decline of rural America, **ABA recommends that the final regulation <u>also</u> include as "underserved" any rural area that has been targeted by a governmental agency for development AND any rural area or county defined by Community Development Financial Institutions Fund regulations as a CDFI investment area.**

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[6] According to the Agencies' proposal, under the definition of a LNMI census tract in the CRA regulations, 57 percent of non-metropolitan counties have **no** LMI tracts, compared to 13 percent of metropolitan counties. The reason for this disparity is that rural census tracts are drawn over relatively large geographic areas, often having relatively heterogeneous populations that, when averaged, tend toward the middle. This leads to a concentration of 72 percent of rural census tracts in the middle-income category, which leaves a small share (15 percent) in the LMI categories. Moreover, because most rural counties have relatively few census tracts, the relatively few LMI rural census tracts are distributed unevenly among rural counties. As would be expected, they also appear to be distributed unevenly among bank CRA assessment areas. About 42 percent of non-metropolitan assessment areas reported by large banks in 2003, compared to 14 percent of the metropolitan assessment areas they reported, lacked such tracts.

<u>4. The effect of certain credit practices on a bank's CRA rating.</u> As we wrote in the prior interagency CRA proposed rulemaking, the proposed adoption of regulatory language providing that a CRA rating may be adversely affected by discriminatory, illegal, or abusive credit practices largely only codifies the CRA Q&A and examination practice. The CRA regulations provide that evidence of discriminatory or other illegal credit practices adversely affect an evaluation of an institution's CRA performance and may affect the rating, depending upon consideration of factors specified in the regulations. Interagency guidance states that this provision applies when there is evidence of certain violations of law, including certain violations of the Equal Credit Opportunity Act, Fair Housing Act, Home Ownership and Equity Protection Act, Real Estate Settlement Procedures Act, Truth in Lending Act, and Federal Trade Commission Act. The Agencies propose to include this language in the regulation.

The Agencies also propose to clarify that an institution's CRA evaluation also can be adversely affected by evidence of discriminatory, other illegal, and abusive credit practices by any affiliate, if any loans of that affiliate have been considered in the CRA evaluation pursuant to __.22(c)(1) and (2). Loans by an affiliate currently are permitted to be included in an institution's evaluation of one of its assessment areas only, and the proposal would be similarly limited to affiliate lending practices within any assessment area. Since the Agencies do not have to permit institutions to claim affiliate lending for CRA credit, requiring institutions to be evaluated on all of the lending of the affiliate in the institution's assessment area that the institution has opted to include for its CRA rating does not seem to be excessive.

The original proposal by the Agencies was broader, and raised a number of concerns. However, the Agencies have revised the proposal and largely addressed our concerns. Nonetheless, each of these laws already contains specific penalties and corrective provisions to protect consumers. While some violations do affect the provision of credit, some violations seem more technical or even unrelated to any CRA concern. For example, errors in providing rescission notices do occur, but rarely, if ever, are they part of a pattern or practice of abuse. Rather they are inadvertent or result from systems failures. Nonetheless, the strict provisions of the Truth in Lending Act will result in extension of the rescission period or even penalties against the bank. Additional punishment of the bank by downgrading the bank's CRA rating not only appears to be a double punishment but also appears to be irrelevant to whether the bank is helping to meet the credit needs of the community. This is particularly true because any violations found by examiners or the bank that might downgrade the CRA rating will be corrected under the provisions of the Truth in Lending Act. However, the Agencies appear to be intending to apply such downgrades in CRA rating only when the actions of the bank or its affiliates truly merit such a step, and **ABA supports the proposal.**

Conclusion

ABA is deeply concerned that the Agencies' proposal actually provides little of the needed regulatory burden relief or rationalization of the CRA regulations needed for community banks. Thus, ABA recommends raising the small bank threshold to $1 billion and strongly recommends raising the streamlined examination threshold to $500 million. ABA supports the replacement of the large bank test for institutions over $500 million with an intermediate small bank examination that uses the streamlined small bank test factors plus a Community Development factor, but the CD factor should not be a separate test. ABA supports enlarging the definition of "community development." The present definition literally causes bank disinvestment from rural communities, and this needs to be corrected. Finally, ABA supports the inclusion in the regulation of the right of the Agencies to downgrade a CRA rating for certain discriminatory credit practices by the bank or by affiliates for lending in the bank's assessment area, when the affiliate's lending was included in the CRA examination at the option of the bank. Given the complexity of the questions posed by the Agencies, the Agencies well may have questions about these comments. If so, please call the undersigned.

Sincerely,

Paul Alan Smith

Paul A. Smith
Senior Counsel