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Comment of Legal Scholars on OCC's Community Reinvestment Act ANPR (Docket ID OCC-2018-0008)


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Comment of Legal Scholars on Docket ID OCC-2018-0008

Submitted electronically

Legislative and Regulatory Activities Division
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Dear Sir or Madam:

Thank you for the opportunity to comment on the advance notice of proposed rulemaking (ANPR) titled “Reforming the Community Reinvestment Act Regulatory Framework,” Docket ID OCC-2018-0008. We are legal scholars specializing in financial regulation and its effect on reinvestment in underserved communities.*

In this ANPR,¹ the Office of the Comptroller of the Currency (OCC) invites public comment on potential revisions to the rule implementing the Community Reinvestment Act (CRA).² The stakes of this ANPR are high, because of the positive effect this landmark piece of legislation has had on revitalizing America’s distressed neighborhoods and communities.³ As the OCC

* Our affiliations are for identification only and do not necessarily represent the views of Boston College.

¹ Office of the Comptroller of the Currency, *Reforming the Community Reinvestment Act Regulatory Framework: Advance notice of proposed rulemaking*, 83 Fed. Reg. 45053 (Sept. 5, 2018) [hereinafter ANPR].

² 12 U.S.C. §§ 2901-2908.

³ See, e.g., Eric Belsky, Michael Schill & Anthony Yezer, *The Effect of the Community Reinvestment Act on Bank and Thrift Home Mortgage Lending* (Joint Center for Housing Studies of Harvard University 2001); Raphael Bostic & Hyojung Lee, *Small Business Lending Under the Community Reinvestment Act*, 19 CITYSCAPE: A JOURNAL OF POLICY DEVELOPMENT AND RESEARCH 63, 64-65 (2017) (reviewing literature); Lei Ding & Leonard Nakamura, “Don’t Know What You Got Till It’s Gone” – *The Effects of the Community Investment Act on Mortgage*

contemplates amendments to the CRA rule, we urge it to build on this success by preserving CRA's traditional emphasis on local communities while expanding CRA to address new ways of banking.

More than two decades have elapsed since the major 1995 rule⁴ that revamped the examination criteria for CRA to reward performance over documentation and effort. Under the 1995 rule, as amended, federal banking regulators evaluate an insured depository's CRA performance based on its delineated assessment area or areas, which are defined according to where the bank⁵ has its main office, branches, automated teller machines (ATMs), and certain surrounding areas.

Since that time, technological and legal developments have allowed banking to transcend its former geographical boundaries. Online and mobile banking allows customers to transact business in the virtual world and some banks have no branches at all. The old barriers to interstate banking fell following the passage of the Riegle-Neal Interstate Banking and Branching Efficiency Act.⁶ Meanwhile, the consumer lending operations of many banks serve far-flung states outside their branch networks and CRA assessment areas.

It would be a mistake to conclude from these developments, however, that brick-and-mortar bank branches are a thing of the past. As we explain in Section II.A below, depositors continue to rely heavily on bank branches. That fact, combined with the CRA's express statutory directives, needs to inform any revisions to the CRA rule going forward. If the CRA rule is amended, it should be done in such a way to maintain banks' responsiveness to the communities served by their branches and ATMs, while also evaluating retail activities of banks outside their branch networks. This additive approach recognizes current banking developments while honoring the statutory language of and Congress' intent behind the Community Reinvestment Act.

I. The Statutory Language of the Community Reinvestment Act

Any analysis of the Community Reinvestment Act starts with the statute's words. As its central command, CRA charges each Federal financial supervisory agency as follows:⁷

Lending in the Philadelphia Market (Fed. Res. Bank Phila. Working Paper 17-15, 2017); John Fitzgerald & Samuel P. Vitello, *Impacts of the Community Reinvestment Act on Neighborhood Change and Gentrification*, 24 HOUSING POLICY DEBATE 446 (2014) (reviewing literature); Daniel Ringo, *Mortgage Lending, Default, and the Community Reinvestment Act* (Fed. Res. Bd., June 15, 2017).

⁴ 60 Fed. Reg. 22156 (May 4, 1995). In 2005, the OCC, the Board of Governors of the Federal Reserve System, and the Federal Deposit Insurance Corporation adopted a joint final rule liberalizing the examination criteria for intermediate small banks (with total assets of between \$250 million and \$1 billion, adjusted annually for inflation). *Community Reinvestment Act Regulations, Joint final rule of the O.C.C., Federal Reserve System, and the F.D.I.C.*, 70 Fed. Reg. 44256 (2005).

⁵ In this comment, we use the word "bank" to refer to any type of insured depository institution. See 12 U.S.C. §§ 2901(a), 2902(2), 2903(c)(3)(C) (applying CRA to "regulated financial institutions" and defining them as "insured depository institutions," as defined in 12 U.S.C. § 1813(c)(2)).

⁶ Pub. L. No. 103-328, 103d Cong., 2d Sess. (1994).

⁷ 12 U.S.C. § 2903(a). CRA defines the "appropriate Federal financial supervisory agencies" as the OCC, the Federal Reserve Board, and the Federal Deposit Insurance Corporation. *Id.* § 2902(1). In this letter, we refer to these three agencies as the "federal banking regulators."

- (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; and
 - (2) Take such record into account in its evaluation of an application for a deposit facility by such institution.

Other provisions of CRA elaborate on the meaning of this provision.

On reading CRA in its entirety, three statutory directives stand out. First, Congress, in CRA, tied the obligation of banks to serve the credit needs of their communities to the physical geographies where their deposit facilities are located. Second, serving the convenience and needs of communities includes providing both deposit services and credit services. Finally, CRA expressly requires serving the needs of low- and moderate-income (LMI) neighborhoods, consistent with safety and soundness.

A. Directive One: CRA Requires Service to Physical Neighborhoods and Communities Surrounding Branch Networks

The statutory language of CRA makes clear that Congress expected banks to serve the convenience and needs of the physical neighborhoods and communities that surround their branches and ATMs. This appears clearly in the part of CRA that requires federal banking regulators to evaluate each bank’s CRA performance “separately for each metropolitan area *in which a [bank] maintains one or more domestic branch offices.*”⁸ Similarly, CRA’s findings expressly state that “regulated financial institutions are required by law to demonstrate that their *deposit facilities* serve the convenience and needs of the communities in which they are chartered to do business.”⁹ As this reference to “deposit facilities” indicates, the express text of CRA establishes that banks owe their core CRA obligations to the areas served by their branches and ATMs.

Other provisions in CRA buttress the conclusion that banks must serve the credit and deposit needs of the physical areas surrounding their branches. For example, Congress emphasized a focus on place when it told federal banking regulators to “encourage” banks “to help meet the credit needs *of the local communities in which they are chartered* consistent with the safe and sound operation of such institutions.”¹⁰ The words “local communities” underscore CRA’s non-negotiable command to serve the physical areas and surrounding geographies where a bank’s branches and ATMs are found. In another provision, Congress allowed any bank that

⁸ *Id.* § 2906(b)(1)(B) (emphasis added). *Accord, id.* § 2906(d) (describing the method of CRA evaluation for banks that maintain “domestic branches in 2 or more States . . .”). CRA defines “domestic branch” to mean “any branch office or other facility of a regulated financial institution that accepts deposits, located in any State.” *Id.* § 2906(e)(1).

⁹ *Id.* § 2901(a)(1) (emphasis added).

¹⁰ *Id.* § 2901(b) (emphasis added). *Accord, id.* § 2903(b) (allowing CRA credit for investments in minority- and women-owned banks, “provided that these activities help meet the credit needs of *local communities* in which such institutions and credit unions are chartered”) (emphasis added).

predominantly serves members of the military “who are not located *within a defined geographic area*” to define its “entire community” to include “its entire deposit customer base *without regard to geographic proximity*.”¹¹ By negative implication, this provision requires other banks to define their assessment areas in terms of “geographic proximity” to their deposit customer bases and assumes that those customer bases are located “within a defined geographic area” or areas.¹²

Together, these provisions make abundantly clear that banks *must* serve the local neighborhoods and communities where their branches are located. CRA does not preclude giving credit for serving other communities that are outside of banks’ branch networks. However, banks that have branches cannot receive CRA credit unless they first discharge their core responsibility to serve areas in “geographic proximity” to their branches.

B. Directive Two: Serving the Convenience and Needs of Communities Includes Both Deposit Services and Credit Services

CRA establishes a general duty on the part of depository institutions to “serve the convenience and needs of the communities in which they are chartered to do business.”¹³ The statute then defines “the convenience and needs of communities” to include “the need for credit services as well as deposit services.”¹⁴ Consequently, offering both types of services is necessary to fulfill a bank’s CRA commitment.

C. Directive Three: CRA Requires Banks to Serve the Needs of Low- and Moderate-Income Neighborhoods

Finally, service to the low- and moderate-income (LMI) segment of communities is intrinsic to every bank’s CRA commitment. This appears in CRA’s language that directs federal banking regulators to assess each 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 . . .”¹⁵

¹¹ *Id.* § 2902(4) (emphasis added).

¹² Elsewhere, CRA directs federal banking regulators to examine the record of banks in serving “low- and moderate-income *neighborhoods*,” *id.* § 2903(a)(1) (emphasis added), demonstrating again that CRA’s core commands require service to real neighborhoods with streets and physical addresses. *Accord, id.* § 2906(a)(1) (requiring federal banking regulators to prepare written evaluations of each bank’s “record of meeting the credit needs of its entire community, including low- and moderate-income *neighborhoods*”) (emphasis added).

¹³ 12 U.S.C. § 2901(a)(1).

¹⁴ *Id.* § 2901(a)(2).

¹⁵ *Id.* § 2903(a)(1) (emphasis added). *See also id.* § 2906(a)(1) (requiring federal banking regulators to prepare written examination reports of each institution’s “record of meeting the credit needs of its entire community, *including low- and moderate-income neighborhoods*”) (emphasis added); *id.* § 2903(d) (instructing federal banking regulators, during their CRA examination of each bank, to “consider, as a factor, low-cost education loans provided by the financial institution to *low-income borrowers*”) (emphasis added).

CRA's emphasis on LMI neighborhoods is a response to historic redlining and seeks to correct the market imperfections that lead to disinvestment in those neighborhoods.¹⁶ Lending, by definition, involves predictions about the risk of default and collection. In poorer neighborhoods, it may be more expensive for conventional lenders to distinguish between low-risk and high-risk borrowers. Often, loan officers are unfamiliar with the profit-making opportunities in poor communities because they do not live in those communities and come from more affluent and privileged social milieus. Greater outreach and education may be needed to reach potential borrowers. Loans may require greater monitoring in order to assure repayment. Borrowers who in fact are creditworthy may not be able to satisfy conventional underwriting criteria, such as long employment with one employer, stable residence at one address, prior credit history, etc. Because loans in such neighborhoods tend to be smaller, moreover, the fixed costs of community reinvestment loans may have to be spread over a smaller potential return.¹⁷

To compound matters, as lenders shun poor neighborhoods, information costs rise. By necessity, current appraisals, which are crucial to evaluating collateral, must be based on prior sales. If house sales in a neighborhood drop due to a lender's refusal to lend, there will be fewer sales to provide a yardstick for future appraisals. Appraisals will become less and less reliable and lenders will become even more reluctant to lend, triggering a downward spiral in investment.¹⁸

Without investment, properties in LMI neighborhoods will continue to deteriorate, spawning negative externalities that will discourage loans throughout the neighborhoods, no matter how sterling an individual borrower or property. If a neighborhood is in physical decline, a lender may decline to lend even where the collateral supports the loan, because future deterioration in the neighborhood could cause collateral values to fall. The result can be a self-fulfilling prophecy, as one reluctant lender makes other creditors reluctant to lend and more and more properties fall into disrepair due to paucity of rehabilitation loans.¹⁹

One way to reverse the problem of information costs in lending is through coordination among lenders. However, such coordination may be illegal and, at a minimum, is legally risky due to antitrust concerns.³⁰ As with cartels, moreover, coordination creates inherent incentives to cheat that make coordination unstable over time.³¹ Another approach would be to foster specialized

¹⁶ See notes 37-49 *infra* and accompanying text. This analysis of disinvestment is excerpted from PATRICIA A. MCCOY, *BANKING LAW MANUAL: FEDERAL REGULATION OF FINANCIAL HOLDING COMPANIES, BANKS AND THRIFTS* § 8.04 (Lexis 2d ed. 2000 & 2014 cum. supp.).

¹⁷ See, e.g., Michael S. Barr, *Access to Financial Services in the 21st Century: Five Opportunities for the Bush Administration and the 107th Congress*, 16 NOTRE DAME J.L., ETHICS & PUB. POL'Y 447, 534-44 (2002); Michael Klausner, *Market Failure and Community Investment: A Market-Oriented Alternative to the Community Reinvestment Act*, 143 U. PA. L. REV. 1561, 1568 (1995); Christopher A. Richardson, *The Community Reinvestment Act and the Economics of Regulatory Policy*, 29 FORDHAM URB. L.J. 1607, 1614-16 (2002); Peter P. Swire, *The Persistent Problem of Lending Discrimination: A Law and Economics Analysis*, 73 TEX. L. REV. 787, 818-19 (1995).

¹⁸ See Klausner, *supra* note 17, at 1569-70.

¹⁹ See Barr, *supra* note 17, at 540; Keith N. Hylton & Vincent D. Rougeau, *Lending Discrimination: Economic Theory, Econometric Evidence, and the Community Reinvestment Act*, 85 GEO. L.J. 237, 256-67 (1996); Klausner, *supra* note 17, at 1570-71; Lawrence J. White, *The Community Reinvestment Act: Good Intentions Headed in the Wrong Direction*, 20 FORDHAM URB. L.J. 281, 284-85 (1993).

³⁰ See Hylton & Rougeau, *supra* note 19, at 257; White, *supra* note 19, at 285.

³¹ See Hylton & Rougeau, *supra* note 19, at 257-58; Klausner, *supra* note 17, at 1577.

markets in which a handful of lenders specialize in loans to poor neighborhoods, thereby developing sufficient expertise and market share to make those loans economically profitable. Tragically, however, this market materialized disastrously in the form of subprime mortgage lending, which triggered the 2008 financial crisis and high rates of foreclosure.²⁰

In sum, reliance on private solutions to the collective action problems posed by disinvestment has proven unworkable at best and catastrophic at worst. CRA fills this vacuum in important ways, by reducing the information costs of healthy credit in LMI neighborhoods. In the process, CRA has helped reverse the added negative externalities that flow from disinvestment and revitalize our nation's urban cores.

In sum, CRA's three statutory directives, when read together, establish the threshold requirements that every bank must meet to satisfy its CRA obligations. These requirements are as follows and frame the content of any amendments to the rule implementing CRA:

- (1) Banks must serve the convenience and needs of the geographic areas surrounding their brick-and-mortar branch offices and ATMs;
- (2) Serving the convenience and needs means providing both deposit services and credit services; and
- (3) Banks must serve low- and moderate-income neighborhoods in order to serve convenience and needs.

II. Response to the ANPR

The three statutory directives of CRA – serving local communities, providing deposit *and* credit services, and emphasizing services to LMI neighborhoods – are the *sine qua non* of any future revisions to the CRA rule. In this section, we describe in greater detail how these three directives frame the contours of any future CRA rule. In the course of our discussion, we will also respond to key issues posed by the ANPR.

First, though, we wish to applaud the OCC's ANPR for taking the values reflected by CRA's directives seriously. The ANPR contains a valuable description of recent market developments as well as a number of good ideas. In other respects, the ANPR handles certain issues in ways that pose concerns. We turn to these topics now.

A. Any New Rule Must Keep CRA's Focus on Local Communities

Our review of CRA's statutory requirements leads to the inescapable conclusion that service to local communities must be the core focus of every bank's CRA evaluation. In CRA, Congress *required* banks to serve the convenience and needs of the neighborhoods and communities surrounding their brick-and-mortar branches and ATMs. Any amendment to the CRA rule must

²⁰ Federal banking regulators have been reluctant to award CRA credit for subprime mortgage loans. Darryl E. Getter, *The Effectiveness of the Community Reinvestment Act 10-12* (Cong. Research Serv. Report No. 7-5700, Jan. 7, 2015).

observe this requirement.

We appreciate, of course, that the business of banking has exceeded the old geographic boundaries of banks to an extent that was unimaginable to Congress when it enacted CRA in 1977. At the same time, brick-and-mortar branches remain indispensable to bank customers. Indeed, just last month, the Federal Deposit Insurance Corporation (FDIC) reported that almost three-fourths of banked households surveyed in 2017 had “used bank tellers to access their accounts in the past 12 months.”²¹ *More depositors used bank tellers than any other method of accessing their transaction accounts*, including automated teller machines (ATMs) or kiosks, telephone banking, online banking, and mobile banking.²² This is not surprising because branches and ATMs are the main way customers deposit checks and withdraw cash. Branches are also where bank customers generally go when they want personal banking services. Conversely, branches are the place where the loan officers of the bank come to know specific communities and neighborhoods.

Given these modern realities and the statutory text of CRA, any new rule will need to strike a proper balance between the geographic expansion of banks’ activities beyond their branch networks and a locally-based approach to CRA. The way to do this is to make any new CRA rule *additive* in nature. Under that approach, every bank with branches would have a core responsibility to serve the convenience and needs of the neighborhoods and communities in geographic proximity to their branches and ATMs. Once that duty was fulfilled, banks could receive extra credit for other CRA activities outside of those locales, whether those activities take place in other states or in the virtual context. In this way, a new CRA rule would fulfill CRA’s statutory requirements while encouraging CRA service in other underserved geographies. Any other approach would pose the danger of inadvertently rewarding banks for branch closures, which would be highly damaging to LMI communities.

B. Serving the Convenience and Needs of Customers Located Beyond the Current Assessment Areas

CRA’s text is similarly instructive about how and when to grant credit for CRA activities beyond a bank’s branch footprint. The statute requires federal banking regulators to evaluate a bank’s CRA performance based on its service to low- and moderate-income neighborhoods and communities. Accordingly, serving LMI communities and households should be the goal of any new approach to CRA credit for activities outside of a bank’s current assessment areas.

Today, the banking landscape features a number of new business models that did not exist in 1977, when CRA was enacted. Many medium-sized and larger banks have hybrid models, with branch networks in some areas but loan production elsewhere. Other banks maintain branches in defined areas but offer expanded geographic coverage through online or mobile banking. At the far end of the technological spectrum, purely online banks have no physical presence except for their headquarters and instead conduct their retail business online or through mobile apps. Industry loan companies and wholesale banks also often conduct far-flung operations from a

²¹ Federal Deposit Insurance Corporation, FDIC National Survey of Unbanked and Underbanked Households 25 (2018), <https://www.fdic.gov/householdsurvey/2017/2017report.pdf> [hereinafter FDIC Unbanked Study].

²² *Id.* at 25-26 & tbl. 4.2.

small geographic base.

Any new rule that gives credit for CRA activities outside of the traditional assessment areas surrounding branches and ATMs should place top priority on service to LMI neighborhoods, communities, and individuals. In particular, banks should be rewarded for extending service to LMI areas and families that have been underserved. These are just some of the areas of need in LMI communities that CRA could address:

- *The so-called “banking deserts”*: Banking deserts are geographic areas that suffer from inadequate bank service.²³ Some banking deserts lack enough investment in community development; others have a paucity of bank branches and are predominated by fringe banking providers such as check cashers and payday lenders. An absence of bank branches can cause banking deserts to fall outside of traditional CRA assessment areas and escape CRA coverage.

Banks should be rewarded under CRA for searching out banking deserts and providing them with bank services. Banking deserts present prime opportunities to expand deposit-taking, including through innovative channels such as mobile banking. Bank deserts often offer profitable lending and other investment opportunities that have been overlooked. Accordingly, these areas are ripe with opportunities to fulfill CRA’s mandate to provide both deposit and credit services.

- *Banking the unbanked*: In 2017, an estimated 6.5% of U.S. households were unbanked because they did not have a deposit account.²⁴ An updated CRA rule could help address this problem by giving CRA credit to banks for successfully assisting unbanked households to open bank accounts.

Attracting the unbanked into the banking system presents a special opportunity for banks that offer mobile banking, given the rapid growth in mobile banking in recent years.²⁵ The experience with “underbanked” customers suggests that mobile banking has untapped potential for recruiting unbanked customers to open bank accounts. Households that are underbanked—meaning that they have transaction accounts but also use one or more fringe banking services—use mobile banking at a higher rate than fully banked households.²⁶ These underbanked households are predominantly low- or moderate-income, as is true for the unbanked.²⁷ Together, these facts suggest that mobile banking could provide a useful point of entry to assist the unbanked to become part of the banking system.

²³ See, e.g., Donald Morgan, Maxim Pinkovskiy & Bryan Yang, *Banking Deserts, Branch Closings and Soft Information*, LIBERTY STREET ECONOMICS blog (March 7, 2015).

²⁴ FDIC Unbanked Study, *supra* note 21, at 2 tbl. ES.1.

²⁵ The percentage of households using mobile banking jumped from 23.2% in 2013 to 40.4% in 2017. *Id.* at 5 tbl. ES.3.

²⁶ *Id.* at 27 tbl. 4.4

²⁷ See *id.* at 19-20 tbls. 3.2-3.3.

- *Helping LMI families build savings:* In 2017, four out of ten U.S. adults reported that they did not have enough money to pay for a \$400 unexpected expense.²⁸ This lack of emergency savings becomes increasingly prevalent as one goes down the income spectrum.²⁹ Even modest amounts of savings could noticeably improve the financial security of these families while helping them avoid getting saddled with debt. Banks that help LMI families in building savings would help address this problem and should be rewarded with CRA credit.
- *Rural areas:* CRA tells federal banking regulators to conduct separate CRA analyses “for each metropolitan area in which a regulated depository institution maintains one or more domestic branch offices.”³⁰ This focus on metropolitan areas traditionally has caused many rural areas to be omitted from CRA assessment areas. Both of us come from families in largely rural states – Kansas and Louisiana – and we have seen first-hand the poverty and lack of bank services and investment in rural communities. If CRA credit is expanded beyond the current traditional assessment areas, service to rural areas should be rewarded.

In conclusion, any amendment to the standard for evaluating CRA performance by banks should condition CRA credit for activities outside of a bank’s traditional assessment areas on satisfactory service to the neighborhoods and communities adjacent to their branches. Assuming the bank has fulfilled this core responsibility under CRA, we would support extra credit for qualifying CRA activities in other geographies, so long as the objective of those activities is to serve low- and moderate-income neighborhoods, communities, and families.

C. A Single CRA Ratio

In the ANPR, the OCC elicited comment on whether the agency should create a metric-based performance measurement system that aggregates an institution’s CRA lending, investments, and services into a single ratio.³¹ The ANPR states: “In a metric-based framework . . . the benchmarks representing the dollar value of CRA-qualified activities could be compared to readily available and objective criteria, such as, a percentage of domestic assets, deposits, or capital from the bank’s balance sheet, to calculate a ratio that could correspond to the benchmark established for each rating category.”³² For each bank, such a ratio would look like this:

$$\frac{\text{Total CRA lending} + \text{total CRA investments} + \text{total CRA services}}{\text{Balance sheet measure (either total assets, deposits, or capital)}}$$

²⁸ See BOARD OF GOVERNORS OF THE FEDERAL RESERVE SYSTEM, REPORT ON THE ECONOMIC WELL-BEING OF U.S. HOUSEHOLDS IN 2017, at 21 (May 2018), <https://www.federalreserve.gov/publications/files/2017-report-economic-well-being-us-households-201805.pdf>.

²⁹ See FDIC Unbanked Study, *supra* note 21, at 44 tbl. 7.1.

³⁰ 12 U.S.C. § 2906(b)(1)(B).

³¹ Under the current CRA rule, small banks only undergo a lending test. Intermediate small banks are also evaluated on the extent and quality of their community development activities, while large banks are assessed under the lending, investment, and services tests. ANPR, *supra* note 1, at 45055.

³² *Id.* at 45057.

We have a number of grave concerns about reducing a bank's CRA evaluation and rating to one number.

The first concern is legal. As mentioned above, CRA expressly requires federal banking regulators to evaluate a bank's CRA performance "for each metropolitan area in which" it "maintains one or more domestic branch offices."³³ The single ratio formula above does not account for individual metropolitan area performance; indeed, it does not even mention it.³⁴ Thus, for banks operating in multiple metropolitan areas, any switch to a single ratio method would violate CRA's statutory requirement to evaluate CRA performance one metropolitan area at a time.

This problem is more than just a legal concern. One of the reasons that Congress required federal banking regulators to evaluate CRA performance for each metropolitan area where a bank has branches is to ensure that banks make CRA commitments to each of the communities where they have offices. A single ratio test would overturn that incentive and encourage banks to cease their CRA activities in many communities that they now currently serve.

Similarly, the single ratio test does not separately evaluate successful CRA activities under each of the three tests (lending, investment, and service). Presumably, under the ratio, a bank that did \$9 million in CRA investments would produce the same numerator as a bank that did \$3 million each in CRA loans, investments, and services. That would have the unfortunate effect of encouraging banks to take the easy route by loading up on big, splashy loans and investments to satisfy the numerator in the place of labor-intensive retail loans and deposit-taking services. Contrast that with the OCC's current practice for small banks, in which a bank must meet or exceed the lending test in order for its community development investments and services to be considered for an outstanding rating.³⁵

Meanwhile, using a balance sheet measure such as total assets, deposits, or capital as the denominator has problems of its own. Today, banks originate most of their loans and other credit receivables for distribution via securitization. That allows them to remove those assets from their balance sheets. Any metric in the denominator that is limited to the balance sheet will consequently understate most banks' asset activities. This would artificially inflate the CRA ratio and thereby allow banks to earn satisfactory or outstanding CRA ratings with less CRA activity than they need today.

In another concern, the numeric benchmark approach would likely cause banks to do just enough qualifying CRA activities to hit their target benchmark and no more. The ANPR suggests that numeric "thresholds or ranges (benchmarks) [would] correspond to the four statutory CRA rating categories."³⁶ It is well known that numeric benchmarks create an "anchoring effect," by

³³ 12 U.S.C. § 2906(b)(1)(B).

³⁴ Further, no mathematical weighting system could fix this problem. Imagine, for example, that one assessment area received a weight of 1 and another assessment area that was ten times more populous received a 10. By increasing its qualifying CRA activities in the larger area, a bank could zero out its qualifying activities in the smaller area without reducing its ratio. By failing to serve the smaller community, this would violate the intent of CRA.

³⁵ ANPR, *supra* note 1, at 45055.

³⁶ *Id.* at 45056.

effectively signaling a maximum that actors must attain in order to meet their obligations. In this way as well, the single ratio approach would likely reduce the current level of CRA activity.

Finally, the single ratio proposal raises a larger philosophical concern. Specifically, do regulators, banks, and the public at large have enough insight into the convenience and needs of diverse communities from Alaska to Maine to set *ex ante* quantitative ratios for CRA performance? Is certainty and mathematical precision worth the cost of losing local responsiveness and less CRA activity? We firmly believe it is not.

D. Consideration of Discrimination and Illegal Credit Practices in CRA Evaluations

Traditionally, federal banking regulators have taken evidence of unlawful credit practices and illegal discrimination based on prohibited categories such as race or ethnicity into consideration in CRA evaluations and ratings. There are strong historical and practical reasons for doing so and we urge the OCC to continue that practice in any prospective CRA examinations and CRA rule.

To understand the importance of continuing this practice, some history is in order. Congress enacted CRA against the backdrop of blatant housing and lending discrimination in the United States.³⁷ Much of this discrimination had been sanctioned by the federal government.³⁸ Beginning in the late 1930s, the Federal Home Loan Bank Board and the Federal Housing Administration (“FHA”) had discouraged black entry into white neighborhoods by using race-based appraisal standards in FHA underwriting guidelines for federally insured mortgages.³⁹ The FHA did not eliminate race-based standards from its underwriting criteria until the 1960s, when it was required to do so by Executive Order 11,063 in 1962.⁴⁰

In addition, the FHA had required the use of racially restrictive covenants in all FHA-guaranteed real estate transactions, thereby perpetuating racial segregation and all-white enclaves. This practice officially ended in 1947, but racially restrictive covenants remained on the books and bolstered racial segregation in housing for decades to come.⁴¹

By the 1960s, the tragic consequences of officially sanctioned mortgage discrimination had become painfully apparent to Congress. Middle-class whites, with the aid of federal subsidies for interstate highways, mortgage insurance and mortgage loans, had beaten a path to the suburbs, leaving poor blacks and other impoverished minorities to languish behind in inner-city ghettos.⁴² At the same time, lenders increasingly refused to make mortgages or small business loans in designated nonwhite communities, a notorious practice known as redlining.⁴³

³⁷ The following discussion is excerpted from MCCOY, *supra* note 16, § 8.04[1].

³⁸ See Swire, *supra* note 17, at 793-99.

³⁹ FHA, UNDERWRITING MANUAL ¶ 937 (1938) (quoted in Stephen M. Dane, *Eliminating the Labyrinth: A Proposal to Simplify Federal Mortgage Lending Discrimination Laws*, 26 U. MICH. J.L. REFORM 527, 535 (1993)).

⁴⁰ 3 C.F.R. § 652 (1959-63), *reprinted as amended in* 42 U.S.C. § 1982. See generally Dane, *supra* note 39, at 536, 539.

⁴¹ See, e.g., Dane, *supra* note 39, at 535-36.

⁴² See, e.g., Swire, *supra* note 17, at 798-99.

⁴³ See, e.g., Dane, *supra* note 39, at 536-37.

The deterioration of the inner city cores and urban unrest finally goaded Congress into action and caused it to enact a suite of federal laws which included CRA. Congress took the first step to address redlining and discriminatory credit denials in 1968, when it prohibited discrimination in housing finance in Title VIII of the Civil Rights Act.⁴⁴ The following decade, as urban neighborhoods continued to decline, Congress passed three more statutes, the Equal Credit Opportunity Act of 1974 (“ECOA”),⁴⁵ the Home Mortgage Disclosure Act of 1975,⁴⁶ and CRA in 1977. All four statutes were designed to address the twin ills of discrimination and disinvestment.

When Congress enacted CRA, one of its two chief concerns was to end redlining.⁴⁷ Although redlining mostly targeted LMI neighborhoods, historically, that redlining was motivated by racial and ethnic discrimination and was strongly correlated with ethnicity and race.⁴⁸ Indeed, for this reason, redlining is not just a central concern of CRA but also violates the fair lending laws.⁴⁹ As this demonstrates, CRA’s focus on LMI neighborhoods is inextricably linked to problems of unlawful housing and credit discrimination.

In acknowledgment of this history, federal banking regulators adopted a joint interagency rule in 2005 stating that “evidence of discriminatory or other illegal credit practices in any geography by the bank or in any assessment area by any affiliate whose loans have been considered as part of the bank’s lending performance” will adversely affect a bank’s CRA evaluation.⁵⁰ As part of their CRA evaluations, the OCC and the other federal regulators also prohibit banks from delineating assessment areas based on illegal discrimination.⁵¹ To carry out these regulations, whenever possible, the federal banking regulators conduct CRA examinations and fair lending examinations together in order to detect the presence of any discriminatory practices.⁵²

These antidiscrimination provisions in the CRA rule are highly important and we urge the OCC to retain them. For all intents and purposes, positive CRA ratings are “Good Housekeeping” seals of approval by the federal government for good community reinvestment performance. Banks with satisfactory or outstanding CRA ratings can tout this federal imprimatur to the public and receive favorable handling in their applications for deposit facilities and for financial holding company status based on the public portion of their CRA examination reports.

⁴⁴ Pub. L. No. 90-284, 82 Stat. 81 (1968) (codified as amended at 42 U.S.C. §§ 3601-31).

⁴⁵ Pub. L. No. 93-495, 88 Stat. 1500, 1521-25 (1974) (codified as amended at 15 U.S.C. §§ 1691-1691f).

⁴⁶ Pub. L. No. 94-200, 89 Stat. 1124 (1975) (*codified as amended at* 12 U.S.C. §§ 2801-2810).

⁴⁷ *See, e.g.*, Getter, *supra* note 20, at 1.

⁴⁸ *See, e.g.*, Ben Horowitz, *Fair lending laws and the CRA; Complementary tools for increasing equitable access to credit* (Fed. Res. Bank of Minneapolis, March 8, 2018).

⁴⁹ *See id.*

⁵⁰ *See, e.g.*, 12 C.F.R. § 25.28(c)(1). In its CRA examination of Wells Fargo Bank, N.A., as of September 30, 2012, for instance, the OCC gave Wells Fargo outstanding ratings on its lending and investment tests and a high satisfactory rating on its service test, yet an overall “needs to improve” CRA rating because of the bank’s lending discrimination settlements. *See* OCC, Community Reinvestment Act Performance Evaluation as of September 30, 2012: Wells Fargo Bank, National Association 4, <https://www.occ.treas.gov/topics/compliance-bsa/cra/2012-55-wells-fargo-cra-evaluation.pdf>

⁵¹ *See, e.g.*, 12 C.F.R. § 25.41(e)(2).

⁵² For a general discussion of the symbiosis between fair lending examinations and CRA examinations, see Horowitz, *supra* note 48.

For this reason, CRA ratings require due diligence by federal banking regulators to rule out unlawful discrimination or credit law violations. If a bank received a salutary CRA rating but was later to found to have engaged in unlawful discrimination or illegal credit practices, that would undermine CRA's objectives. Further, it would put federal banking regulators in the uncomfortable position of awarding CRA credits only to later to unearth unlawful discrimination or illegality at the bank in question. For these reasons, the anti-discrimination provisions of the CRA rule are of vital importance and must be continued.

E. The Importance of a Joint Interagency Rule

Finally, we urge the OCC to redouble its efforts to promulgate a joint interagency rule with the Federal Reserve Board and the FDIC. Going it alone would have several deleterious effects.

First, separate rules for the OCC and the other two agencies would undermine one of the OCC's own goals, which is to increase the certainty surrounding CRA evaluations.⁵³ With warring standards, bank holding companies with state and federal depository institution charters would be subject to different CRA approaches, depending on the subsidiary. Local governmental and non-profit institutions that partner with banks would similarly have enormous confusion about which CRA standards applied.

Second, the ANPR does not consider the effect of separate CRA rules on merger application decisions by the Federal Reserve Board. Numerous national banks owned by bank holding companies regularly engage in mergers. In bank merger applications that also result in the merger of the parent holding companies, the Federal Reserve must evaluate whether convenience and needs would be served.⁵⁴ We doubt that the Federal Reserve would abandon its own method for evaluating convenience and needs in merger applications and nothing in a separate OCC rule would prevent it from doing so. In this additional way, two separate approaches to CRA compliance would confuse the marketplace and increase the uncertainty surrounding bank mergers and the conditions on those approvals.

Lastly, if the OCC rejects a joint interagency approach, it will create an unlevel playing field for state-chartered banks and thrifts. That is a dangerous path to tread, as the lead-up to the 2008 financial crisis showed.⁵⁵ We urge the OCC to work with its fellow regulators to find common ground and avoid that unfortunate outcome.

⁵³ While we appreciate that the flexibility of the current CRA rule engenders some uncertainty, that uncertainty does not hurt most banks' CRA ratings. Economist Darryl Getter reported, for instance, that each year from 2006 through 2014, approximately 97% or more of banks received CRA ratings of satisfactory or higher. Getter, *supra* note 20, at 9. If anything, this "Lake Wobegone" effect suggests that CRA standards need to be tightened, not loosened, as the single ratio proposal would potentially do.

⁵⁴ 12 U.S.C. § 1842(c)(2) ("In every case, the Board shall take into consideration the financial and managerial resources and future prospects of the company or companies and the banks concerned, and the convenience and needs of the community to be served").

⁵⁵ See generally KATHLEEN C. ENGEL & PATRICIA A. MCCOY, THE SUBPRIME VIRUS: RECKLESS CREDIT, REGULATORY FAILURE, AND NEXT STEPS (Oxford University Press, 2011).

Thank you for the opportunity to share our thoughts on the OCC's ANPR.

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