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SPECIAL FEATURE

OCC Launches CRA Modernization

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The first overhaul of Community Reinvestment Act (CRA) regulations in a generation began with the Office of the Comptroller of the Currency's (OCC) publication of an advanced notice of proposed rulemaking (ANPR) Sept. 5.

The final policy could reshape how banks finance affordable housing and other community development activities.

The OCC is one of three federal agencies responsible for CRA. OCC oversees national banks, the Federal Reserve Board supervises state-chartered banks that are members of the Federal Reserve System and the Federal Deposit Insurance Corporation (FDIC) examines other state-chartered banks. It is unusual for one agency to go it alone on a major regulatory initiative, suggesting that the Fed and FDIC are not yet on board, but OCC hopes the three agencies will unite when it's time to propose a specific plan.

Current CRA policy favors affordable housing and other community development activities. Large banks undergo a three-part examination covering lending, investment and service. Community development lending is a required component of the lending test and the investment test has helped to drive banks' participation in low-income housing tax credits (LIHTCs), new markets tax credits (NMTCs) and historic rehabilitation tax credits (HTCs). The Comptroller of the Currency, Joseph Otting, has said CRA focuses too much on affordable housing and mortgage lending, proposing greater emphasis on such other activities as small-business lending, student loans and church-sponsored activities.

CRA modernization is long overdue. When the current rule took effect in 1995, interstate banking was in its infancy and Internet banking and mobile banking was a distant vision. Affordable housing and community development conditions and practices have evolved substantially as well. Although the banking agencies pledged back then to revisit the CRA rules within five years, they have made only minor changes. The banking agencies last considered significant changes to CRA guidance in 2010, when they jointly conducted a series of hearings, but ultimately decided to leave the regulation intact, instead preferring only to clarify some technical interpretations since then.

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Comptroller Otting has taken a more ambitious approach, promising to make CRA more clear, predictable, transparent, flexible and simple. An important element would be to accommodate banks' increasing use of online and mobile channels to serve customers.

OCC's biggest idea is to base a bank's CRA rating on a single ratio, comparing its total CRA-related activity to some measure of its size, such as its domestic assets, deposits or capitalization. Separate subcategories for lending, investment and service might or might not be continued. Under the plan, a bank would know in advance how much financing is enough to satisfy its CRA obligation. Many questions arise about how it would work.

- Can one size fit all banks? Could the same yardstick measure performance for banks with different business strategies, product mixes, sizes, locations and charters? For example, would banks in different parts of the country be expected to reach the same ratio? How about banks having a wide or narrow array of financing products?
- If a bank knows how much financing is enough to get a satisfactory CRA rating, will it be less motivated to strive for an outstanding rating? Virtually all banks currently receive at least satisfactory ratings.
- How would banks' CRA strategies change if they are no longer required to make investments or community development loans? If the objective is to reach a dollar volume target as easily and profitably as possible, would banks favor scalable financing requiring the least additional work, risk and commitment of capital–such as purchasing Fannie Mae, Freddie Mac and Ginnie Mae securities over more meaningful but smaller, more complex activities that could tie up more capital for longer terms? Would rural areas and smaller metropolitan areas receive fair attention? Would certain preferred activities get extra credit and would that be enough to affect a bank's rating and therefore its strategy?
- How would the particular needs and circumstances of different communities be considered? Under CRA, banks are supposed to be responsive to the needs of their communities, but assigning weights to various activities in every metropolitan area and rural community would be difficult to calibrate and very complicated. Similarly, if home prices and mortgage amounts in Chicago are twice as high as in Toledo, Ohio, is it fair that the average mortgage in Chicago should contribute twice as much to a bank's CRA volume target as the average mortgage in Toledo? For that matter, should a much larger mortgage to a high-income condominium buyer in a gentrifying neighborhood in Brooklyn or Seattle count even more? Moreover, the CRA statute requires a separate rating for each metropolitan area and each state where a bank has a branch or other deposit-taking facility, but would these state and metro ratings even matter in a single-ratio rating structure?
- How would the service test be incorporated into the single ratio? Currently, the CRA service test includes the distribution of a bank's branches, the degree to which it serves low- and moderate-income deposit account customers, account features to accommodate these customers and volunteer activities such as serving on the boards of nonprofit community development organizations. The ANPR suggests that volunteer hours could be assigned a dollar value, but does not address other service elements. And how would a bank with many branches be compared with an internet bank?
- How high would the target ratios be set and how often would they change? Would the target be set so roughly the same share of banks receives an outstanding rating? In response to the criticism of some community groups that virtually no banks receive unsatisfactory ratings, would the threshold for satisfactory ratings be raised? Could the next

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comptroller of the currency simply decide to raise or lower the ratio?

In addition to the single ratio, the ANPR also raises other issues important to affordable housing and other kinds of community development.

Under current CRA policy, consideration for activity beyond a bank's assessment area is both limited and uncertain, making it difficult for banks to participate in national financing pools. For example, community development financing may be considered in a broader regional area if a bank has been responsive to its assessment area, but there is no clear standard for measuring that responsiveness and no clear definition of a regional area. The effectiveness of this policy is limited because banks need to know whether an activity will be considered when they are deciding whether to finance it, not when the bank is examined years later. How will a revised CRA regulation retain a focus on communities where banks have branches while accommodating activity elsewhere?

Finally, OCC expressed an interest in providing more clarity about what activities will be considered. For example, the current treatment of unsubsidized but affordable rental housing–which comprises 80 percent of all affordable rentals in the United States–remains vague. Policy guidance places a burden on banks to provide a market analysis for each loan or investment sufficient to convince an examiner years after the fact that low- or moderate-income renters are likely to occupy a property, but no criteria or standards are provided.

The public has until Nov. 19 to comment on OCC's ANPR. Changes in the assessment area definition could improve LIHTC equity pricing in underserved areas but an expanded range of CRA-eligible investments could decrease the demand for the LIHTC and new markets tax credit. The OCC hopes to have a final rule in place next year. There is much work to do to ensure that a modernized CRA will continue to expand economic opportunity for low- and moderate-income people and communities. ❖

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