Overhaul of Anti-Redlining Law Sparks Rift Among Financial Regulators

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By Renae Merle, The Washington Post, December 13, 2019

A proposed overhaul of a 40-year-old anti-redlining law has created a rift between three powerful financial regulators.

The Office of the Comptroller of the Currency (OCC) and the Federal Deposit Insurance Corp. (FDIC) have unveiled an ambitious plan for updating the 1977 Community Reinvestment Act, which would give the banking industry new flexibility on meeting government-mandated goals for investing in poor neighborhoods.

But the Federal Reserve has, so far, refused to sign on to the proposal.

If not resolved, the rift could leave some of the country's thousands of banks complying with one set of rules while their competitors face others.

"Although the Federal Reserve Board has not joined the proposal at this time, I appreciate their engagement and recommendations for improvement, many of which are reflected in this proposal, and I look forward to continuing to work with them as the proposal moves forward," Jelena McWilliams, chair of the FDIC, said this week as the agency's board voted to move forward with the proposal.

The Federal Reserve has not said why it is balking at the plan, but two people familiar with the discussions, who spoke on the condition of anonymity because they were not authorized to speak publicly, said the powerful regulator questioned whether there was enough data used to form some of its underpinnings.

"Any modernization of the Community Reinvestment Act must further the goal at the heart of the statute — encouraging banks to meet the credit needs of local low- and moderate-income communities," the Federal Reserve said in a statement. "We look forward to studying the public comments on the rule proposed by the OCC and FDIC. At this time, no decisions have been made about how the Federal Reserve will proceed."

Meanwhile, the OCC and FDIC are moving forward with a proposal that could transform the billions a year banks make in loans to low-income communities. Democrats and community groups are warning that it could significantly weaken the landmark legislation, while the banking industry has called it a long-overdue update to an aging law.

Here are key parts of the proposal by the FDIC and OCC.

A question of geography
Key to the Community Reinvestment Act is geography. The 1977 law was passed to address redlining, a practice in which banks refuse to extend loans in certain poor communities or charge those borrowers more.

Under the current rules, federal regulators judge banks on the types of loans and other business they do in places where they have branches, ATMs and other physical operations.

Between 2012 and 2017, banks spent an average of $78 billion a year on community development lending and $55 billion a year on small-business loans in low- and moderate-income neighborhoods that fall under the law, according to the National Community Reinvestment Coalition. Banks were also given credit for billions spent on mortgage loans to low- and moderate-income borrowers in poor neighborhoods.

But the banking industry says the traditional measurements have become outdated as more of their customers have shifted online and the number of bank branches dwindled across the country.

Under the proposal, banks would still be required to lend in lower-income neighborhoods near their branches. But they would also be judged on their activities in the other areas where they have significant customer deposits.

The proposal “recognizes that banks may now receive large portions of their deposits from outside their traditional assessment areas,” McWilliams said during the recent board meeting.

Communities groups say this new flexibility could also allow banks to skirt their core responsibilities under the law while seeking more lucrative work.

“The stated intention is to bring more financing to underserved and rural areas. It is not going to accomplish that,” said Buzz Roberts, chief executive of the National Association of Affordable Housing Lenders. "Instead it is going to add focus on states and metropolitan areas with greater populations like New York, California, Texas. … It is not clear that those states are underserved in general.”

What projects qualify for credit?
Under the proposal, regulators would develop and frequently update a list of commonly approved activities under the law, addressing one of the industry’s chief complaints. Banks would also be able to get preapproval from regulators for Community Reinvestment Act projects they are pursuing.

“We’re encouraged that it would clarify what qualifies for CRA credit,” said Rob Nichols, president of the American Bankers Association.

The plan could also clear the way for banks to get credit for activities the law had traditionally not allowed, including offering mortgages in high-cost areas such as San Francisco and New York or financing multimillion-dollar projects to build child-care facilities or hospitals.

“Everyone is for hospitals, but the proposal [could] cover financing hospitals that don’t particularly serve communities where low- and moderate-income people are concentrated. That has a diluting effect on the broader purpose of the law,” Roberts said.

That may also take banks’ attention away from less profitable affordable-housing projects, he said. “The focus on affordable housing is going to go down.”
That part of the proposal also drew criticism from FDIC board member Martin J. Gruenberg.

It “expands eligible and qualifying CRA activities to include some of what banks already do in the ordinary course of business, thereby diluting the effectiveness of CRA,” he said at Thursday’s board meeting. Gruenberg was the sole FDIC board member to vote against moving forward with the proposal.

What’s next?
The public will have 60 days to comment on the changes proposed by the FDIC and OCC. It could then be revised to reflect any concerns raised or approved early next year.

A key test will be whether the Federal Reserve eventually agrees to adopt the proposal — or develops one of its own. The Fed regulates banks in about 20 percent of the market and the remainder are regulated by the FDIC or OCC.

“We continue to believe that the nation would be best served by a final interagency rule that also includes the Federal Reserve, which would provide a consistent regulatory framework for all banks," said Nichols of the American Bankers Association.