Revamp of Investment Rule Could Benefit Richer Districts

By Jim Saksa, CQ News, Jan. 28, 2020

Before releasing a controversial proposal to overhaul a decades-old law that encourages banks to lend in poor and neglected neighborhoods, Comptroller of the Currency Joseph Otting went on a cross-country tour selling the changes he had in mind.

"While [the Community Reinvestment Act] has driven trillions of dollars in investment since 1977, more needs to be done to ensure banks are motivated to maintain and increase investment, lending and services in rural areas, including Native American communities like the ones we visited today," Otting said during an August visit to Native American pueblos in New Mexico.

The OCC proposal would expand the law's list of qualifying investments to farms, tribal lands and low- and moderate-income tracts within opportunity zones created under the 2017 tax cuts (PL 115-97) — the kind of rural communities that form the backbone of the Republican Party's base.

But community groups and affordable-housing lenders say those newly qualified places will never see the investments Otting has promised because the new rule will also make it easier for banks to focus qualifying loans in bigger, booming cities — the urban and suburban areas that have turned blue in recent years and may put long-held GOP strongholds into play this November.

“Unfortunately, the policy intent to reach into so-called CRA deserts to underserved parts of the country, that's probably not likely to happen under this,” said Benson “Buzz” Roberts, president of the National Association of Affordable Housing Lenders, a trade group of banks and community development financial institutions.

“The comptroller sold this thing to say that places that are ignored — rural places, [Native American] lands, etc. — we're going to make them extra eligible, but they've constructed the thing in such a way that it makes it more likely that capital concentrates in fewer and fewer places,” said Jesse Van Tol, CEO of the National Community Reinvestment Coalition.

Even though the proposal could shift more bank lending into their districts, congressional Democrats have aggressively opposed it.

House Financial Services Chairwoman Maxine Waters, D-Calif., took the unusual step of leading a group of lawmakers to demonstrate opposition to the proposal at the Dec. 12 board meeting where the FDIC voted 4-1 to adopt it. At a Jan. 14 Financial Services subcommittee hearing, Democrats disparaged the proposal as another deregulatory sop to banks and Republicans defended it as a reasonable change to rules written before the rise of online banking — an ironic dynamic that will likely repeat itself Wednesday, when Otting is scheduled to defend it before the full committee.

Promoting growing cities

The CRA was enacted in 1977 to reverse decades of disinvestment in urban areas caused by redlining, a practice of painting minority neighborhoods as no-loan zones. Banks opened branches and took deposits in the neighborhoods but reinvested the money elsewhere. To reverse that siphoning of wealth, the law made serving low and moderate-income areas around their branches a prerequisite for banks seeking regulatory approval for mergers and acquisitions.

Supporters and opponents of the proposed rule agree the law needs updating. Its geographic focus made more sense when regulations were last substantially updated in 1995, before the rise of online banking and a recent uptick in bank mergers. Americans increasingly bank with institutions that don’t have brick-and-mortar branches, undermining the goal of spreading the wealth around.

The OCC proposal would judge some banks in areas where they have significant customer deposits even if they don't have branches there. Banks will naturally have more deposits in major cities, not farming communities, Roberts said.

“The result of the proposal might be to add a little more competition for [CRA-qualifying] activities in New York City and Los Angeles, because if you're now looking at where those branchless banks are really getting their deposits, they're probably getting them from major population centers," he said.

Community groups get a lot of say under the current law. Tailoring to local needs means examiners can’t use uniform tests. The OCC says its proposal will make today’s subjective evaluations more quantitative by putting more emphasis on the total dollar value of a bank’s CRA-qualifying investments as a percentage of assets rather than just its performance in the assessment areas around each branch.

Banks would still be tested on performance in the assessment areas, but the proposed rule says a “significant portion, such as more than 50 percent” would still need good grades in order for the bank enterprise as a whole to pass.

“The corollary is also true: you can fail it in 50 percent of your assessment areas,” Van Tol said.

Consider how a bank with branches in New York City, Baltimore, Richmond and Washington might respond to the change, Van Tol added.

“You could theoretically ignore Baltimore and Richmond, [and] concentrate on New York and Washington, D.C., which are growing markets, [with] a higher percentage of affluent people," he said. "It makes it much easier to cherry-pick CRA opportunities and places where you can earn the most profit for the lowest effort."

At a press conference last week, Otting said the 50 percent threshold wasn't set in stone and argued that the proposed rule would have bank examiners fully review all of a bank's assessment areas, rather than rely on a sampling. Under the current rules, examiners do "full scope" reviews of a subset of a banks' assessment areas and do lighter reviews for the rest.

According to the NCRC, the banking industry made an average $55 billion a year in small business loans in low- and moderate-income neighborhoods and $78 billion a year on community development lending between 2012 and 2017, and billions more in qualifying mortgages.

Political impact

If the critics are correct, the proposed rule may lead banks to concentrate those investments in already booming neighborhoods across the nation.

The information and service sectors that have driven much of the nation's economic growth over the past 20 years have concentrated on larger cities, fueling growth in city centers and their suburbs. But housing costs in cities like New York, Boston and San Francisco have started to price residents out. While those cities have seen populations plateau and even decline, Sunbelt cities have continued to expand at feverish paces.

The fastest-growing metro areas in 2018 were mostly blue Sunbelt cities in red states: Phoenix; San Antonio; Charlotte, N.C.; Austin, Texas; Jacksonville, Fla.; Miami and Las Vegas were all in the top 15. Atlanta; Houston; Raleigh, N.C.; Nashville, Tenn.; and Tampa, Fla., have all seen strong population growth in recent years.

The movers are mostly younger adults looking for the economic opportunities that the coastal cities provide but with cheaper rents. They've found that sweet spot in relatively newer cities throughout the South and West that have room to expand and fit the influx of new residents. And when they move, they bring their more liberal politics with them.

Historically, younger voters lean further left than their elders but fail to show up at the polls. But that changed in 2018, when millennial turnout nearly doubled from 2014 to 42 percent and helped Democrats gain 41 seats in the House.

While Democrats won suburban districts in Orange County, Calif., and around Philadelphia and Chicago, Republicans have solidified their hold on smaller, industrial cities and rural areas that have lagged the rest of the nation, economically. According to a recent New York Times analysis of the 2016 election, Trump won 58 percent of the vote in the counties with the poorest 10 percent of the population.

The proposed CRA changes could accelerate these trends by allowing banks to invest more in growing population centers — loans to small businesses in boomtowns are more likely to be repaid than in struggling Rustbelt cities. That would lead to even more college-educated millennials and Generation Zers to move to increasingly blue metro areas in these red and purple states.

“Banks are going to be given certain dollar volume targets that they have to meet. And the question for the banks is: What is the fastest, easiest, most profitable way to hit those numbers?” said Roberts. “Would you rather make $100,000 loan in some rural community or a $300,000 loan in a major city?”

But the OCC proposal includes an element that could counter that. Current rules give banks CRA credit for home mortgages made in low and moderate-income areas, even when they go to wealthier homeowners. The proposal would end the credit for mortgages to middle- and upper-income individuals; home loans to borrowers who make more than 80 percent of a census tract’s median income would no longer qualify.

But Van Tol noted the proposal increases the size of CRA-qualifying loans to small businesses. Loans to relatively upscale bars and restaurants in gentrifying neighborhoods would still get CRA credit.

It also broadens credit for investments for “naturally occurring affordable housing,” where rents are affordable to low and moderate-income households, but doesn’t require that those units go to lower-income individuals.

“It’s like opening a window while closing a door,” Van Tol said, arguing that many developments in already affordable parts of the country would qualify.