Urban Affairs Coalition
Driving Change from the Ground Up

Community & Economic Development:

1207 Chestnut Street
Philadelphia, PA 19107

Comments Re: Docket No. R-1386
CRA Regulations

August 30, 2010

Ms. Jennifer J. Johnson
Secretary
Board of Governors of the Federal Reserve System
20th Street and Constitution Avenue NW
Washington, DC 20551

Dear Board of Governors:

On behalf of the Urban Affairs Coalition, I appreciate the opportunity to provide written testimony regarding modernization of CRA regulations in order to better fulfill the purpose of the CRA within the contemporary context of financial institutions and low- and moderate- income communities.

The Urban Affairs Coalition is one of the Philadelphia region's largest nonprofit agencies, operating and managing a wide range of programs, services, and public policy initiatives that serve nearly 85,000 people each year. The Coalition drives change from the ground up by strengthening our network of program partners, shaping public policy issues, and delivering programs that respond to urgent community needs. Now celebrating 40 years, the Coalition has worked on diverse issues of access, equity and inclusion. As the organizational vehicle for numerous collaborative initiatives among lenders, community groups and government, we are well positioned to attest to the powerfully positive effects of the CRA on our communities as well as to shortfalls in bringing crucial capital to vulnerable communities.

I want to stress our strong support of the CRA. Research demonstrates that the CRA has contributed powerfully to community development in low- and moderate- income communities. According to data from the National Community Reinvestment Coalition (NCRC), loans to support affordable rental housing, economic development and community projects grew from

$18 billion to $73 billion between 1996 and 2008. The total loans for community reinvestment over the 12-year period equaled $480 billion.

At the same time, changes in lending and the creation of new lending entities have diluted the impact of the CRA. This is why we believe that changes to modernize the CRA and further increase loans in low- and moderate- income communities are needed. Our specific recommendations address five areas: 1) Expanding assessment area coverage; 2) Inclusion of affiliates in CRA exams; 3) Increasing rating classifications; 4) Inclusion of related financial industries ; and 5) Greater emphasis on financial education.

<u>Expanding assessment area coverage:</u> According to NCRC, approximately two-thirds of bank lending is done in markets in which the bank does not have branches and is therefore not subject to CRA scrutiny. The narrow definition of CRA-qualified assessment area provides an incentive for banks to lend outside of their CRA assessment areas, thus undermining the original intent of the CRA. From the community perspective, data demonstrates that banks are more likely to lend to low- and moderate-income borrowers if they are in an assessment area where the bank is subject to CRA scrutiny. Without the CRA requirement, banks tend not to lend to these communities. Therefore, it is in the community's best interest to ensure that all areas where banks lend are considered assessment areas that are subject to CRA.

At UAC, a primary focus of our work is building wealth in low-income neighborhoods. In Philadelphia, nearly one in four of our residents (24.3%) is living below the poverty rate. At the same time, we estimate that, based on HMDA reports, fewer than 25% of the top 306 conventional home purchase mortgage lenders that made loans in the Philadelphia in 2008 had deposit-taking branches that required the lenders to include Philadelphia in their assessment areas. The remaining 75% were either banks from outside the market with no branches in Philadelphia or mortgage banks not subject to the CRA at all. This demonstrates that in a city challenged with a high poverty rate only a quarter of its mortgage lenders are subject to the CRA. There are two reasons for this: 1) the narrow definition of assessment area coverage, and 2) the definition of what kinds of lending institutions come under the CRA mandate.

Our recommendations is that the application of CRA responsibility apply to <u>all</u> markets in which a significant percentage of the bank's lending takes place – 5% or more – and not be limited to where banks have deposit-taking branches. In the world of modern finance, the link between deposits and lending is not the crucial factor that it was when the CRA was implemented in 1978 and the regulations should be revised to reflect this fact.

<u>Inclusion of affiliates in CRA exams</u>: Related to the expansion of the assessment area is inclusion of affiliates in CRA exams. Currently, it is an option of the bank to include the lending of a corporate affiliate that is under the same holding company in the bank's CRA examination. As big bank holding companies often have separate corporate arms for different types of lending (i.e. subprime), they only opt to include them in their CRA exams when it would benefit their rating classification. Predictably, this allows a bank to hide from scrutiny those activities that are contrary to the spirit of the CRA. As with the assessment area issue, this is a gaping loophole that creates an incentive for banks to shift lending capital from CRA-subject lines of business to lines of business that are not subject to CRA. **The Coalition supports the proposal to automatically include all corporately affiliated institutions in CRA examinations**.

<u>Increasing rating classifications:</u> The present four-tier CRA performance evaluation system is too narrowly defined by passing or failing. Given that the consequences of failing are harsh, examiners are understandably reluctant to fail a bank. This has resulted in an extremely high percentage of passing grades (over 95%). **A larger number of rating classifications with a**

continuum of consequences, both positive and negative, would create a fairer evaluation system for banks, as well as be more supportive of community interests and needs.

Inclusion of related financial industries: Assuming the purpose of the CRA is to ensure equitable opportunities for people in low- and moderate-income areas to access credit and financial services, we believe it is no longer appropriate to limit the regulations only to depository institutions. With non-CRA regulated institutions now making two-thirds of housing related loans, the case is strong that **all housing and commercial lenders should be subject to the CRA**.

Greater emphasis on financial education: The Coalition seeks to build bridges between mainstream financial institutions and low- and moderate- income communities for loans and financial services. Until the current financial crisis, the emphasis was on extending the bank side of the bridge by encouraging banks to apply more flexible underwriting standards. Now, with bank lending becoming so conservative, we have necessarily begun working to enable borrowers to become more bankable through financial education and counseling. From a policy perspective, the challenge is to acknowledge and reward banks for supporting financial education without diminishing the mandate to lend. **Financial education should receive greater value for CRA compliance purposes because it has become so essential to assuring the flow of credit to low- and moderate-income communities. We want to stress, however, that we are not recommending that financial education replace the weight placed on lending.** Otherwise, banks might be inclined to establish unattainably high underwriting standards, and, when lending in LMI areas drops disproportionately, banks could point the finger at borrowers for not qualifying.

In closing, I want to reiterate the Coalition's strong support for the CRA and the impact it has on the healthy development of low- and moderate-income communities. We believe that by addressing the areas discussed above, the CRA would be able to more effectively fulfill its purpose by being better aligned with modern financial structures.

Thank you for the opportunity to submit these comments.

Sincerely,

Donald C. Kelly
Director of Community and Economic Development