PUERTO RICO BANKERS ASSOCIATION

May 16, 2013

VIA ELECTRONIC MAIL

Mr. Robert de V. Frierson
Secretary
Board of Governors of the
Federal Reserve System
20th Street and Constitution Avenue NW
Washington, DC 20551

Re: Community Reinvestment Act: Interagency Questions and Answers Regarding Community Reinvestment Act Docket No. OP-1456

Dear Mr. de V. Frierson:

The Puerto Rico Bankers Association[1] ("PRBA") respectfully submits to the Board of Governors of the Federal Reserve System ("FRB") this letter with its comments in connection with the revision of the Interagency Questions and Answers Regarding Community Reinvestment Act proposed by the FRB, the Federal Deposit Insurance Corporation ("FDIC") and the Office of the Comptroller of the Currency ("OCC") ("collectively, the "Agencies"). PRBA's comments specifically relate to the proposed question §___.12 (t)-9, which addresses the quantitative consideration given to a certain type of community development investment (the "Q&A").

In connection with the Q&A, the Agencies have requested comments particularly in regards to:

- Whether the proposed Q&A is sufficiently clear.
- Whether the proposed Q&A will encourage or discourage investments or loans in organizations with a community development mission.
- Whether the proposed Q&A provide the flexibility necessary to encourage community development activities, whether direct, indirect or through the provision of capital investments, in connection with an organization with a primary purpose of community development.

The PRBA respectfully submits that by making it final, the Q&A will impair the ability of financial institutions in Puerto Rico to comply with the

[1] The PRBA represents the seven (7) commercial banks doing business in Puerto Rico, all of which are FDIC insured banks. One (1) of the banks represented by the PRBA is a FRB member bank and one (1) is a national bank supervised by the OCC.

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investment requirements[2] of the Community Reinvestment Act (12 U.S.C. 2801 et seq. (the "CRA"). Furthermore, the Q&A will have a detrimental effect on the various community development organizations in Puerto Rico that depend on the structured transactions described below, to fund its community development related activities, and thus, on the community needs of Puerto Rico in general.

In essence, the Q&A provides that if a financial institutions invests in (or lends to) an organization that, in turn, invests those funds in instruments that do not have community development as their primary purpose and uses only the income or a portion of the income, from those investments to support the organization's community development purposes, the Agencies will consider only the amount of the investment income used to benefit the organization or activity that has a community development purpose for CRA purposes.

The structured transaction funding mechanism which serves as the backbone of widely recognized community development organizations in Puerto Rico consists of a transaction where an interest rate spread is derived from the difference of the coupon payment of the underlying collateral placed by the organization and the coupon payment of the structured note issued by the organization. The interest rate spread sacrificed by the investor financial institution is the resulting spread that is received as interest income by the organization with the established frequency ("Structured Transaction").

Before discussing the specific aspects on which the Agencies have requested comments, we consider it necessary to provide the Agencies with a description of the local economic and market conditions that have significantly limited the CRA related investment opportunities for our member banks and a description of the community development organizations that significantly depend on the Structured Transactions for their funding needs.

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[2] CRA requires the Agencies to assess the banks' performance in meeting the needs of their assessment area through qualified investments. These investments are defined as any lawful investment, deposit, share or grant with a primary purpose of community development as defined by CRA.

Puerto Rico has been experiencing a deep economic recession during the past seven (7) consecutive years. Everything seems to indicate that the situation in Puerto Rico is not necessarily a consequence of a global recessionary cycle but instead, that the local problem has an important structural component. For the first time in modern history, declines in economic activity have been recorded for seven (7) consecutive years and the economy of Puerto Rico fell by more than 3.5% in the period 2010-2011. Furthermore, the amount of public debt in Puerto Rico has increased steadily over the last few years, and in fact, has exceeded the annual growth rate of the Nominal Gross National Product in 15 of the 20 years between 1990 and 2010. According to data from the Puerto Rico Planning Board, the island is fast approaching its maximum debt capacity, since for every dollar produced 95 cents are owed to various sources of financing. In the United States, this indicator stands at approximately 65 cents on every dollar. The data suggests a pattern that is unsustainable in the long term.

Ratings for Puerto Rico government issued bonds have deteriorated and only a few CRA qualified issuances have been out to the market during the past five (5) years. According to the Government Development Bank, 93% of the funds raised through the Government's most recent bond issuances has been used to cover operational expenses or refinance old debts, activities that have no effect on increasing the economy's productive capacity. Moreover, liquidity of the Puerto Rico Government Development Bank is currently seriously compromised.

Due to the adverse economic situation, the government of Puerto Rico has eliminated many incentives for low or moderate income first home buyers that helped create a secondary market for CRA related investments.

Furthermore, other federal investment opportunities targeting Puerto Rico are few and national level CRA Funds scarcely benefit the Puerto Rico region.

Due to all the above discussed factors, CRA qualified investments have become scarce in Puerto Rico.

If the Q&A is made final, the ability of our banks to comply with the investment requirements of the CRA, will be significantly impaired. As mentioned before, when compared with the United States market, the

Puerto Rico market has limited opportunities for CRA investments that would be acceptable investments under the banks' investment policies. The PRBA and its membership have been trying to move away from a dependency and charity model and envision a collaborative model where banks partner with stronger, financially diverse and sustainable nonprofit organizations in community development projects that truly impact the quality of life of low and moderate income families and individuals in Puerto Rico. Up to two or three years ago, local banks relied on governmental transactions, mostly related to affordable housing at the state level, as well as other general obligations and municipal bonds pertaining low and moderate income community infrastructure improvements. In this respect, the PRBA is proud to have contributed in the creation of the Structured Transactions as a CRA investment mechanism that allows organizations exclusively devoted to community development in Puerto Rico to issue debt and negotiate with our banks as a means to raise much needed capital for their community development endeavors.

On the other hand, should banks in Puerto Rico be discouraged from entering into Structured Transactions most if not all of the not-for-profit community based organizations that have been structured to use such mechanism for their funding, will be significantly and adversely impacted.

Our banks have invested over $150 million in the below mentioned community based organizations, all of which significantly depend on Structured Transactions to fund their operations. The FDIC has consistently supported our local bank's Structured Transactions to such community based organizations and have regarded them as being "innovative". Following is a brief description of such organizations and quotes of excerpts of FDIC comments on the CRA public evaluation reports relating to Structured Transactions by some of our banks involving such organizations.

1. The Puerto Rico Housing and Human Development Trust Fund (FIDEVI by its Spanish acronym).

   FIDEVI is a charitable, irrevocable and perpetual trust fund created under Deed of Trust dated May 5, 2004, among the Governor of Puerto Rico, the President of the Puerto Rico Bankers Association, the

President of the Puerto Rico Mortgage Bankers Association and three (3) representatives of the homeless advocacy community.

FIDEVI is the product of a collaborative alliance between Puerto Rico's banking industry and the homeless population advocacy community with the commitment of the Government of Puerto Rico. The purpose for which FIDEVI was created is to devote its corpus and income to the promotion and support for the development, rehabilitation and preservation of adequate, affordable and accessible housing for people of limited, scarce or no economic resources in the Commonwealth of Puerto Rico. FIDEVI has been funded through the structured transaction mechanism pursuant to legislation approved by the Legislature. FIDEVI would be left with scarce or no funding for its operations if the local financial institutions are discouraged from investing in FIDEVI as a consequence of the Q&A.

Following are FDIC comments regarding a Structured Transaction by one of our banks with FIDEVI:

"In early 2011, [Banco Santander de Puerto Rico] purchased two additional investments in newly offered charitable arbitrage offerings. The first investments involves a charitable trust that was initially created in May 2004. This trust was established for the purpose of financing and developing housing for high risk individuals, including homeless, mentally ill, AIDS patients, elderly, addicts, and other alienated populations. The overall goal of this fund is to facilitate the construction of 400 homes per year, for rent or for sale at considerably low prices. In accordance with the mission of the trusteeship, 80 percent of the funds will be used for homes targeted for individuals that meet less than 50 percent of median family income (low-income), while the remaining 20 percent will be targeted for individuals whose incomes are greater than 50 percent, but less than 80 percent (moderate-income). SBPR's initial investment in this entity is $15.0 million."

2. Patronato de Monumentos de Viejo San Juan

The Patronato de Monumentos de San Juan, Inc. is an entity organized under the laws of the Government of Puerto Rico. Its purpose is to collect charitable contributions and resources to be used to finance the restoration and maintenance of the San Jose Church of Old San Juan. The Department of the Treasury has ruled that the organization is exempt from the imposition of Puerto Rico income taxes pursuant to Section 1101(4) of the Code, as a charitable organization. Its mission is to repair, restore and maintain the most important historical and architectural gothic style construction from the 16thcentury and to open it fully to the public after being closed for more than thirteen years. By way of Law 195 of December 23, 2009, the Patronato de Monumentos de San Juan, Inc. can offer tax-exempt issues for the sole purpose of raising capital for San José Church restoration and maintenance.

The San José Church Restoration Project, thru Patronato de Monumentos de San Juan, Inc. (the "Patronato"), will revitalize the Northern part of Old San Juan and will play a pivotal role in making local government efforts to renovate the area a success. By restoring this historic, religious and cultural landmark, the Patronato will contribute to the economic and tourism growth of the area, including La Perla which is a very low income community adjacent to the project. The Patronato's integration to local and central government plan to renovate the Old San Juan district is essential.

Following are FDIC comments regarding a Structured Transaction with Patronato:

"In March 2011, the bank in a charitable offering under the laws of Puerto Rico, that has as its ultimate goal to issue up to $100 million in notes to various investors. Monies from this fund will initially be used for the restoration of an historical gothic structure in Old San Juan. Restoration of this structure will increase and expedite the rehabilitation of the area, enhance economic development, and assist in the completion of the master urban plan to revitalize the city. This restoration project will have an immediate impact on the local community by creating 100 direct and indirect jobs, many of which will be filed by low-and moderate-income people. Upon completion of the project, another 30 permanent jobs are expected to be created. Also anticipated as a consequence of this restoration project is the reintegration of the local La Perla community and

its inhabitants. La Perla is a slum aside of the northern historic city wall of Old San Juan that has always been known of its high rate of illegal drug trafficking and crime. Ongoing projects within the scope of the urban master plan call for new development to include roadways, a waterfront promenade, and a light rail system."

3. Puerto Rico Conservation Trust Fund ("Conservation Trust")

Conservation Trust is a charitable, irrevocable and perpetual trust fund created under Deed of Trust dated January 23, 1970 among the Governor of Puerto Rico, the Secretary of the Interior of the United States of America and the Administrator of Puerto Rico Economic Development Administration to implement a joint plan to help develop and preserve the natural resources of Puerto Rico. Conservation Trust operates as a not-for-profit institution under a designation from the United States Internal Reserve Service pursuant to Section 501(c) (3) of the Internal Revenue Code of 1986, as amended. The principal purpose of Conservation Trust is to protect and enhance the natural resources and beauty of Puerto Rico. Conservation Trust has implemented its purpose through the acquisition, active management and development of lands possessing great ecological, aesthetic or historical value in Puerto Rico. Conservation Trust holds these properties in perpetuity for the benefit of the people of Puerto Rico. Conservation Trusts demonstrate its commitment to the community through a series of educational programs for community economic development directed at children, youth and adults of low income communities in the surroundings of its properties. Most of the products sold at their premises are locally made by small farms and artisans.

On Conservation Trust, the FDIC has indicated as follows:

"In prior years Doral Financial Corporation (DFC), the parent company of DB, issued senior and subordinate notes to a state run conservation trust fund, wherein this same trust fund sold bonds in the capital markets which was collateralized by these same subordinate notes. The interest yield spread

(approximately $2.0 million) between these subordinate notes paid by DFC and the interest paid by the conservation trust fund bonds (arbitrage interest) is then utilized by the trustees of the fund to finance the operational expenses of said fund. The purpose of this fund is to protect and enhance the natural resources and beauty of Puerto Rico. Through this charitable fund, the acquisition of lands, as well as the active management and development of such lands that possess ecological, aesthetic, and historical value to the island and the people of Puerto Rico is protected in perpetuity. Since the establishment of this trust, approximately 23,000 acres of land in 24 different locations throughout the island have been held for conservation. The educational aspect of this program impacts many people throughout the year, including students, teachers, and non-profit entities. As part of the trust's educational program, these groups received the necessary training regarding capacity building, productive use of the lands for gardening and food production, and the value of the ecosystems, especially since approximately 80 percent of the food consumed by the Puerto Rico population comes from imports. Since most of the properties are located in the more economically depressed rural areas of the island, these programs offer an opportunity to contribute to the surrounding communities, by offering these individuals and families the necessary skills to develop their own income producing opportunities. As part of the trust program, approximately 50 workshops are conducted each year to train local residents in the basic skills of purposeful land use and food production. The amount of such donated interest during the current evaluation period amounts to approximately $6.1 million."

4. Sociedad de Educación y Rehabilitación de Puerto Rico ("SER")

SER (Puerto Rico Educational and Rehabilitation Society), operate as a not-for-profit institution under a designation from the United States Internal Revenue Service pursuant to Section501(c) (3) of the United States Internal Revenue and Section 1101.01 of the Puerto Rico Internal Revenue Code of 2011, as amended.

SER was founded in 1950, as an affiliate of the National "Easter Seals". The first Rehabilitation Center opened in 1954. Currently, SER is the only organization in Puerto Rico that simultaneously provides rehabilitation services and education to children with disabilities from kindergarten through high school using a regular academic curriculum that facilitates successful empowerment and community inclusion. Of the 123 students total served annually, 80% of students' families earn $40,000 or less for a 2-5 family, 60% come from low income families according to HUD's housing income limits standards, and 53% are poor according to the Department of Education standards

Today, SER is currently the only Pediatric Physical Medicine and Rehabilitation Center operating on the island in an integrated and personalized manner, with clear objectives to achieve independence, productivity and efficiency of each participant treated and his or her family, including but not limited to providing medical, therapeutic, psychological, educational and support services.

Since 1978, SER's programs and services are accredited by the Commission on Accreditation of Rehabilitation Facilities, Medicare, the Department of Health, the Department of Education and the Higher Education Council.

Pursuant to certain laws of the Commonwealth of Puerto Rico, interest paid by SER on its debt obligations is exempt from Puerto Rico tax. SER has not yet entered into any Structured Transaction. However, due to the need to diversify its sources of funding, SER has been actively pursuing opportunities to enter into Structured Transactions with our banks.

5. Punto Verde, Inc. P.T. ("Punto Verde")

Punto Verde is a Puerto Rico workers-owned special corporation organized under the Puerto Rico General Corporation Law, as amended. Punto Verde overseas the construction, management and operation of a children's park located in the Luis Muñoz Marín Park, in San Juan, Puerto Rico (the "Children's Park"). The Children's Park

integrates both recreational and educational elements emerging from its central theme of nature, offering pleasant entertainment for children and the entire family. Special care is taken to make facilities accessible to handicapped persons, both children and adults. The Children's Park also intends to serve as a model of a community-based profitable business venture by providing persons from the eight very low income communities bordering the Caño de Martín Peña an opportunity to participate in the operation of the Children's Park.

With respect to Structured Transactions involving Punto Verde the FDIC has indicated the following:

"In September 2006, the bank purchased $3.0 million of a Puerto Rico Tax Exempt Note (2006 Series A). The proceeds of this note will be reinvested in higher yield investments, the yield of which will be used to operate an interactive recreational park for children in the Luis Muñoz Marin Park. In addition, the goal of this investment is to develop entrepreneurs in the San Juan metropolitan area, providing incubator services for small business for low-income persons who may operate as concessionaires of related business."

Our comments on the specific aspects of the Q&A requested by the Agencies follow.

a. Whether the proposed Q&A is sufficiently clear.

The Q&A appears to be sufficiently clear.

b. Whether the proposed Q&A will encourage or discourage investments or loans in organizations with a community development mission.

The proposed Q&A will greatly discourage, if not completely eliminate, investments in community development organizations that depend on Structured Transactions for their funding needs.

It should be mentioned that, generally, these organizations are created with a minimal capital and, by specific requirements of the trust instruments under which they are created, the trusts funds must be substantially invested in the community related activities for which they were created. Thus, these organizations operate with minimal or no capital. As a consequence, generally, such organizations would not qualify for loans or other credits from banks or other financial institutions. Moreover, neither do these organizations possess adequate collateral to provide as security for a loan or other credit. As a result, the Structured Transactions become the main available alternative for funding for these organizations. In connection with the Structured Transactions, banks are taking the risk, being flexible in the application of their investment policies in order to invest in notes that will undoubtedly benefit the community. Banks' treasurers have been clear that the institutions are entering into these transactions, for the benefit of the community, for CRA compliance and a result of the scarcity of local CRA investments, and not because they are particularly attractive or profitable.

The benefit of these Structured Transactions for the community based organization is that it receives a continuous and stable source of income. However, such income would not be possible unless the financial institution puts at risk a much higher amount which is the equivalent to the total value of the investment. Furthermore, as mentioned before, it is only because the transaction is CRA qualified (qualitative-quantitative), that the financial

institution is willing to enter into the transaction with these organizations, since from a credit and risk management perspective, they would not ordinarily qualify for such credits.

In summary, should the Q&A be made final, the CRA investment market in Puerto Rico will be severely reduced in detriment of the community based organizations that depend on Structured Transactions for their funding needs. As a result, the Q&A will have a devastating effect on the communities served by these organizations.

c. Whether the proposed Q&A provide the flexibility necessary to encourage community development activities, whether direct, indirect or through the provision of capital investments, in connection with an organization with a primary purpose of community development.

We respectfully submit that, as drafted, the Q&A does not provide flexibility to encourage community development activities. The Q&A provides no exceptions for transactions that provide funding to community development organizations that depend to a great extent on Structured Transactions for their funding needs and that would not otherwise qualify for regular credits or loans.

Due to the adverse economic conditions prevailing on the island, the receipt by these organizations of grants or donations or even governmental assistance sufficient in amounts to achieve their purposes, is highly remote. As mentioned before, if the Q&A is made final as proposed, CRA investments for organizations with a primary purpose of community development that depend on Structured Transactions, will be completely eliminated to the detriment of these organizations. The PRBA is deeply concerned with the impact that this situation will have on the present and future of community development initiatives on the island as a whole.

CONCLUSION

We respectfully submit that if made final, the Q&A will have the effect of impairing the ability of financial institutions to comply with the investment requirements of the CRA. Furthermore, this will have the unintended consequence of leaving community based organizations in Puerto Rico without the virtually only source of funding during a period of economic recession on the island.

For the reasons set forth above, the Q&A should be modified to consider the total amount invested by our financial institutions in connection with Structured Transactions entered with community development organizations that depend on such mechanism for their funding needs.

We hereby urge the Agencies to consider the adverse effect that the Q&A would have directly and indirectly on our member bank's ability to comply with CRA investment requirements and on the present and future of community development organizations in Puerto Rico.

The PRBA appreciates the consideration of these comments. Should you have any questions regarding these comments, please do not hesitate to contact the undersigned.

Sincerely,

Arturo L. Carrión
Executive Vice President