Proposal: 1723 (AF94) Reg BB - Community Reinvestment Act

Description:

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Subject: R-1723 Community Reinvestment Act

Comments:

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Revolve Asset Management, the fund manager for Entrepreneur Backed Assets (EBA) Fund, appreciates the opportunity to comment on the Federal Reserve Advance Notice of Proposed Rulemaking (ANPR) regarding the Community Reinvestment Act (CRA). Undoubtedly, CRA has led to significant improvements in access to capital for entrepreneurs in underserved markets. Since 1996, banks have issued almost $2 trillion in small business loans, community development loans, and investments in low-to-moderate income (LMI) communities. Furthermore, in cities across the country, CRA has motivated banks to provide loans to and investments in Community Development Financial Institutions (CDFIs) for economic development.

In order to bolster CRA effectiveness and address changes in the banking industry and advances in technology, it is reasonable for the Federal Reserve to evaluate enforcement modifications. Many of the proposed changes provide needed detail to CRA evaluations, including an increased reliance on data for establishing performance benchmarks.

It is important that the Federal Reserve retains the distinction between large and small banks for CRA examination purposes. The Federal Reserve is seeking public input on the proposed change to asset thresholds for distinguishing small and large banks. The current cutoff is $326M for small banks, with the proposed cutoff at either $750M or $1B. We believe that it is important for the large bank designation to include all banks capable of the activities evaluated under the large bank CRA performance evaluation. The Federal Reserve should consider lowering the proposed asset thresholds to reflect this.

We applaud the Federal Reserve commitment to using data on deposit products for LMI customers in order to set performance thresholds. Under the proposed rule, a bank would earn a satisfactory if its ratio of loans to deposits is 30% of the aggregate ratio. The evaluation would also consider a percent of home loans to LMI borrowers and LMI communities, with a bank receiving a satisfactory if the percentage of loans is 70% of its peers or 65% of the portion of the population that is LMI. Other ratings will also have established ranges in the future. We believe that having clear performance thresholds will help increase the effectiveness of CRA for LMI communities, but also believe that there is insufficient differentiation in ratings despite a clear difference in how banks are working in their communities. When thresholds are set, they should result in outcomes that truly are outstanding for the community, rather than being outstanding in name only. Outstanding banks should likely need to be at more than 120% of peers or the portion of the population (business or individual) to truly deserve such recognition. Satisfactory ratings should also push banks to be closer to 100% for high satisfactory.

We do not support the reduction of subtest ratings from five to four, with the combination of high satisfactory and low satisfactory into one category. This has the possibility of removing much of the nuance that can drive performance in LMI areas. The proposed rule should increase distinction in bank ratings to accurately reflect real performance. Many of the additional measures are evaluated after the bank has passed the Satisfactory mark, making it even more critical to award that rating to bank's with adequate performance regarding LMI populations.

The new test that combines both community development investment and lending provides the options for outstanding financing to be considered alongside new financing that occurred during the CRA exam cycle. We believe that although outstanding financing plays a role in a work in LMI communities, these should remain distinct, with a greater emphasis on new financing. This will encourage banks not to rely on outstanding financing and continue to provide services and support in their communities. We also suggest that this approach be used for the national and assessment area benchmarks used in assessing community development financing performance, with a higher consideration going towards assessment area benchmarks. We do not believe a reliance on new financing will result in short-term financing as the additional work of each new deal will provide a counterweight.

Although the Federal Reserve retains that assessment areas should be based around geographical areas with bank branches, we believe that more consideration should be given to adding assessment areas with large numbers of deposits for institutions that are primarily deposit gathering. National assessment areas for internet banks may be helpful in cases where deposits are not concentrated. Assessment areas for large banks can include a county as the smallest designation, while small banks can designate a portion of a county.

Currently, small business loans are for firms with $1M or less in annual revenue. The Federal Reserve has proposed increasing that threshold to $1.65M to adjust for inflation. Bank lending of small loans under $100,000 has fallen relative to GDP growth and larger loans over the last decade. These smaller loans are particularly important to LMI neighborhoods where businesses tend to be smaller and where margins may not justify larger loans. If the Federal Reserve follows through on the increased threshold, it must not come at the expense of smaller dollar loans, and data analysis of past bank performance evaluations should be done to see if increasing this threshold will allow so many additional loans to count that small dollar loans might suffer as a result. Even as those smaller dollar loans have decreased, there has been no change in the number of banks getting satisfactory.

We support the elimination of the distinction between full-scope and limited-scope assessment areas. Increasing the importance of limited-scope AAs will provide increased importance for smaller metro areas and rural counties, which are often underserved. A bank receives a rating lower than the overall state weighted average in a certain percentage of assessment areas, it cannot receive a higher rating. We believe these two measures will help even performance between geographic areas.

The Federal Reserve proposes several rule changes or additions to attempt to deal with the existence of hot spots and community development deserts. These are admirable and additional effort should be made to try to equalize efforts. With regards to these rule changes, Revolve Asset Management believes some additional incentive to work in CRA deserts would be appropriate. The lack of existence of nonprofits or community partners in certain areas is often due to lack of collaboration and support. Hot spots only became hot spots because of support and nurturing to nonprofits and community organizations looking to support LMI neighborhoods, individuals, and businesses from banks over long periods. To that end, a rule change to address deserts should provide additional ratings boost to commitments that are long-term and sustained, whether that is a 5-year board term at a new nonprofit or a multi-year grant commitment. All multi-year commitments of donations to organizations should be given greater ratings boost as should donations into those community development deserts. Only with long-term, sustained investment will new partners come into being.

The Federal Reserve is the first regulatory agency to propose that violations of fair lending and consumer protection law can result in CRA performance downgrade. We believe that this is an important step forward for accountability.

Many of the changes to CRA evaluation require reliance of deposit data. The Federal Reserve requested comment about the use of deposit data collected by the FDIC. Although the data collected by the FDIC is insufficient for long-term use, we support the use of this data to create performance thresholds until proper collection and reporting processes can be put into place.

Thank you for the opportunity to comment on this proposed rulemaking.

Sincerely,

Revolve Asset Management