February 15, 2021

Board of Governors for the Federal Reserve System
20th Street and Constitution Ave. NW
Washington, DC 20551
Re: **Community Reinvestment Act: Docket No. R-1723 RIN 7100-AF94**

Dear Sirs,

There is an old saying, "Don't let the perfect be the enemy of the good." But the desire to minimize subjective judgment and replace it with scores of metrics can create this very problem and the danger is the Regulation can become so complex it becomes convoluted and confusing. This was one of the problems with the OCC 2020 CRA rule. Rather than clarifying performance expectations and ratings the risk is to make them so complex as to confuse everyone. The ANPR in most respects is far more realistic and practical than the OCC's rule and there are some very good ideas proposed. Nevertheless, there are some concepts expressed in the ANPR that apply to only a very small number of banks, but which will place an unnecessary burden on all banks. A good example is the concept of "deposit-based" assessment areas. The application of this concept will require every bank to geo-code its deposits to determine if more than 50% are derived from outside a bank's assessment area(s). This idea is based on the assumption that changes in technology have resulted in banks attracting a large volume of deposits far removed from the traditional deposit-gathering mechanism, full- and limited-service branches and deposit-taking ATM's. Our experience (and a deposit study we are in the process of completing) indicates that community banks continue to attract the overwhelming percentage of deposits from depositors close to their branch networks. There is no published empirical data we are aware of that substantiate the assumption underlying the proposed deposit-based assessment areas insofar as community banks are concerned. So why adopt such a broad reaching data collection and reporting burden without the evidence to support the reasonableness of such a mandate? Again, there are a number of very good ideas in the ANPR which we strongly support, but there are a few concepts such as the deposit-based assessment areas that we believe are counterproductive and unwarranted. At the same time, in these comments we propose some concepts not contained in the ANPR.

I have been a CRA consultant since 1994. I grew up in a small business family. And I was a banker who specialized in lending to small businesses for 16 years. In 1983, I was named "Small Business Banker Advocate of the Year" in Connecticut by the U. S. Small Business

Administration. That same year I testified in front of the US Senate Small Business Finance Committee as an expert witness on small business finance and the nascent secondary market for SBA loans. I also served two terms as a state senator in Connecticut. So, I think I bring experience from a 360-degree perspective regarding the CRA. I can see the Regulation from the experience of a banker and as a small business owner and as a community leader.

One aspect of the CRA that distinguishes it from any other regulation is that when it is applied as intended CRA performance evaluations measure how well a bank is "meeting the need for credit services" within its Assessment Area(s). In other words, CRA is intended to measure a bank's lending success meeting the community's need for credit services, which is the most significant source of most banks' revenue.

Good CRA performance should be synonymous with strong market performance and profitable lending that benefits the communities served by banks. ***Establishing CRA tests and performance standards that correlate success meeting the credit needs of defined communities with successful banking metrics (such as market rank and share) is sure to gain enthusiastic support from the banking community and communities served by banks (because the public will be able to compare performance among banks active in the assessment area). Performance standards should weave in market rank and market share comparisons which will make the correlation of CRA success and market success more transparent to everyone***. *This alone is a good reason to mandate that all banks held accountable to perform under CRA should be required to report under CRA*. Any bank that takes its CRA responsibilities seriously should be collecting, monitoring, and managing data related to its CRA responsibilities. Uploading that data to regulators will cost nothing for responsible institutions. So not requiring reporting is not helping banks – it is actually hurting banks. Ask examiners who exam non-reporting banks and who must collect loan samples to evaluate CRA performance.

Almost all the goals of the ANPR can be achieved by fine-tuning the existing Regulation without turning it upside down and making it more complex. The following are my comments about proposed changes in the ANPR and my suggestions regarding how the existing Regulation can be vastly improved without making it too complex. A fine tuning of the Regulation may be more effective than a major overhaul. For example, applying the concept of "comparators" with specific quantitative factors (percentages applied to the comparators as proposed in the ANPR) is a simple, but nevertheless big step forward toward quantifying the performance standards which have been too vague for too long. Reporting more information about community development lending and investing would not be a big added burden (for most banks it would mean reporting only a dozen or so transactions), but it would provide big benefits in terms of invaluable performance context information so necessary to form an informed judgment about CRA performance. My comments and opinions are based on more than a quarter of a century of experience advising hundreds of community banks. But I have advised community groups as well.

Finally, I applaud the Board's effort to "modernize" the Regulation. But I think the impact of technology on deposit-gathering has, for most community banks, not precipitated a diaspora of depositors far from the communities where banks have their branches. My company currently is conducting a study of banks regarding the geographic dispersion of deposits and we will share observations with the Board when the results are complete. Please accept my comments below in the spirit they are intended, as constructive suggestions to fine tune the Regulation.

- ✓ **<u>The ANPR proposes a large bank thresholds of $750 million or $1 billion asset size</u>**: We support this standard and even suggest it be reduced to as low as $500 million for reasons we explain below.
  - Almost every bank in the country is accountable to perform under the CRA, but only 10% of banks are mandated to report under the CRA. This is an enormous mistake for several reasons.
  - First, it is nearly impossible to get true "peer" data for the 90% of banks that are not large bank reporters. So, the basis for the aggregate and disclosure data is the performance of only large banks. Community banks should have the opportunity to compare themselves to other community banks, but this is not possible except for the few banks that voluntarily report under the CRA. Moreover, if the main goal of the CRA is "meeting the need for credit services" the best measure of that need is the lending activity reported under the CRA. But omitting the lending activity of small and intermediate-small banks leaves out significant local sources of credit (which in *<u>local credit markets</u>* can be significant). Everyone, including small banks, would be better off if all banks >$300 million were required to report under the CRA.
  - Second, "out of sight, out of mind,": very few non—reporting lenders actually collect and monitor their CRA activity. The result is a "Keystone Cops" drill when a CRA exam is pending. This adds to the difficulty of evaluating performance because examiners must develop a sampling of data upon which an exam will be based. Moreover, a bank in such a situation would have no clue about the accuracy of the sample and would have no way of preparing for examiner questions regarding performance. Non-reporting is a form of regulatory relief that is very harmful to all concerned, including the banks, regulators, and the community.
  - Third, the burden of reporting under the CRA is minimal. The FFIEC provides free software and many small banks generate 100 or fewer small business or small farm loans annually. This means the software cost is zero and the data entry cost is minimal (how much does it cost to enter an average of 2 loans per week?). The benefit of cost savings is far outweighed by the negative consequences of non-

reporting which almost always results in a lack of reliable data about a bank's lending activities.

- We have been consulting with hundreds of community banks regarding CRA for 26 years. Mandating the collection and reporting of CRA data would help thousands of CRA officers help their banks manage their CRA responsibilities and improve CRA performance.

✓ **<u>Assessment Area Configuration flexibility</u>**:

The ANPR proposes that the current flexibility in the Regulation that allows a bank to adjust its Assessment Area to the area it "can reasonably be expected to serve" be changed for "Large" banks that will need to maintain Assessment Areas that include counties or MSA's in their entirety while maintaining the current flexible rule for small banks. The underlying rationale for this reduced flexibility appears to be the Board's intention to establish quantitative performance standards and to make available a "dashboard" so that banks and the public can see what the performance standards are for large banks.

- Current practice as well as the practice proposed in the ANPR is to use "aggregate" data extracted from the annual HMDA and CRA Aggregate & Disclosure files to establish performance standards based on "peer" data, specifically the "penetration rates" in low- and moderate-income census tracts as well as the penetration rates lending based on "borrower characteristics". This data and the penetration rates are readily available for any combination of census tracts. In fact, all commercial CRA software that we know of includes the data and the penetration rates that can be computed from the data for *<u>any combination of census tracts anywhere in the USA and its territories</u>*. My company, which is a small business, does this routinely for our community bank clients. *Any bank of any size can determine the performance standards based on the A&D data for any combination of census tracts*. ***Moreover, GeoDataVision has developed maps that allow us to add and subtract tracts to an Assessment Area and simultaneously, in real time, determine the impact on bank performance and the performance standards derived from performance context***. So why restrict the flexibility currently provided in Assessment Area rules when performance standards derived from the A&D data can be easily computed down to the tract level for any bank? Restricting Assessment Areas to sizes no small than entire counties could be a big problem, particularly for banks under the $2 billion or $3 billion asset-size grouping because they may not have the ability to serve an entire county. Of the roughly 4,200 banks regulated by the FRB and the FDIC about 2,700 had 5 or fewer branches in the 2020 SOD Report. But many of these banks would be included in the "Large Bank" categories proposed in the ANPR. The response may be that examiners would take that into consideration as an important performance context factor, but that subverts many of the main reasons for the changes proposed in the ANPR: to make CRA ratings more transparent, objective, measurable and certain (i.e., no guesswork). Unreasonably large Assessment Areas will precipitate unreasonable performance standards that will be misleading to the public (which does not have the sophisticated understanding examiners have) and accommodating that impact by allowing for subjective judgment by examiners is a complete contradiction of the major objectives of the ANPR. We infer from the ANPR that one reason for inflexible AA configuration is the concept of a "dashboard" that would include quantitative performance standards that banks, and the public could refer to. But, as we stated before, the A&D data and the demographics published by the FFIEC allow the determination of performance standards for any combination of census tracts in real time. There is no need to hogtie banks into a rigid Assessment Area construct when it is easily possible to determine benchmarks in real time using mapping existing mapping technology.

- The proposed restriction of CRA Assessment Areas would be particularly detrimental to a substantial segment of "Large" banks if the thresholds are reduced to $500 million or even $1 billion. There are many banks that would fall into those categories that do not have the branch network to serve counties in their entirety. While examiners may take into consideration the ability to serve the AA to mitigate potential criticism of poor performance caused by unrealistic Assessment Areas this defeats one of the major purposes of the ANPR, the creation of objective and realistic performance measures. Unrealistic Assessment Areas lead to unrealistic performance standards. We have many clients in the $1 billion to $2 billion asset size range that annex parts of counties into their defined communities because those banks know they cannot reasonably be expected to serve some counties in their entirety.
- We have encountered a growing number of banks that are running afoul of the current assessment area delineation restrictions because those banks are pursuing a far reaching market strategy, well beyond conventional markets restricted by bricks and mortar branches, to originate residential mortgages and small business loans using LPO's and other means of distribution, and to fund those activities with secondary market sales in the form of conforming mortgages and/or SBA-guaranteed loans without relying on local deposits except on a temporary basis. Therefore, we applaud the Board's proposal to include LPO's as a factor in facility-based assessment areas. However, there still may be many lenders using the secondary markets who generate lending activity by other means. *We would suggest that loans outside a bank's assessment area(s) sold into the secondary market should be evaluated at value net of sale proceeds for the purposes of computing the assessment area ra*tio.

This value, net of secondary market proceeds, would be computed only for loans extended outside the defined community. For loans within the assessment area the net value calculation would not apply because the community would receive the full benefit of the credit extension, no matter if the loans were funded by local deposits or secondary market sales.

- **Deposit-based Assessment Areas:** The Board has proposed the concept of Assessment Areas based on concentrations of deposits, even if a bank has no branches within or nearby. The Board has proposed this concept because it believes that technology, particularly the Internet, has resulted in deposits being more geographically spread away from the traditional markets served by bricks-and-mortar facilities. There may be some truth to that assumption, but there is no empirical data documenting the extent of the impact of technology and new marketing techniques on the geographic dispersion of deposits. The only official data is in the annual Summary of Deposits Report that is based on branch locations, not depositor locations. Except for Internet Banks and perhaps wholesale and Limited Purpose Banks, it is questionable whether deposits are now more significantly remote from banks' branch systems than in 1977. This is particularly true of local community banks. Only 590 of the nearly 4,200 banks regulated by the FRB or the FDIC had more than $1 billion of assets as of 12/31/2019. Our opinion is the deposit-based Assessment Areas will not affect the vast majority of banks. However, we do point out what we believe is a significant problem with the concept, even for larger banks. If a bank will be held accountable to meet the need for credit services in areas where a bank has no facilities nor personnel, it will be exceedingly difficult for a bank to ascertain the need for credit services and even more difficult to deliver such services to communities remote to the bank's facilities and personnel. Therefore, there should be an adjustment to performance standards in deposit-based AA's if they were to be adopted into a new CRA Rule.
- We have one client bank that is located in a vacation community. They have many seasonal depositors who live far away from the bank's assessment area. This phenomenon may be unique to banks in seasonal communities, but the deposit-based assessment area concept could have very negative implications for banks in such situations. We have encouraged our client to submit comments about this and they have indicated they intend to do so.

✓ **Activity to be measured in CRA Performance Evaluations:**

- The ANPR proposes a "screen test" that would be based on the ratio of local lending activity to local deposits outstanding in an AA. The "threshold" would be established by computing HMDA- and CRA- reported loans originated and purchased by local lenders divided by the outstanding local deposits of those CRA-reporting lenders with the threshold at 30% of the benchmark. This is an interesting attempt to measure the adequacy of a bank's lending within its defined community. We see problems with the proposed benchmark. First, in any market there always is a much higher level of HMDA-reported lending versus deposits than small-business lending compared to deposits. This introduces a bias in favor of mortgage lenders vis lenders that exclusively or primarily extend commercial (small business) loans. Exacerbating this bias is the fact that many more mortgages are sold into the secondary market than small business loans. So, mortgage lenders will benefit from the proposed screen test as modeled while small business lenders will suffer from inherent inequities in the relative relationship between mortgage lending and deposits and small busines lending and deposits. The ANPR proposes setting the screen at a "low level, such as 30 percent of the benchmark" which means only banks that are at extremely low ratios will be disqualified from eligibility for the presumption of "satisfactory" on the Retail Lending subtest in an Assessment Area, but our concern would be that the screen test, if it were to be transparent (and we believe it should be) would potentially establish an unofficial benchmark that could distort the public's perspective on the adequacy of bank lending within an assessment area. We believe the current 50% standard is minimal and reasonable and the current practice of evaluating a bank's market share in the local deposit market as a secondary reference point when a bank falls below the primary Assessment Area ratio is a good approach that has been used for years. If the concept of a loan-to-deposit ratio were to be adopted, we recommend the ratio be adjusted to recognize the significant difference between mortgage volume and deposits outstanding and small business (or small farm) lending and deposits outstanding. GeoDataVision has developed a model that recognizes and balances those two important considerations when examining loan volume in the context of a relationship with the deposit market.

✓ **<u>Performance Metrics:</u>**

- The ANPR proposes **geographic and borrower distribution metrics** that entitle bank to presumption of "satisfactory" rating. This would be *based on the number of loans originated or purchased (not values*). We disagree with the elimination of loan values which is a <u>*true measure of a bank's commitment relative to its resources*</u>. We like <u>*the current balanced approach*</u> that considers both loan counts and loan values. ***Loan counts are an important measure of the breath of the beneficiaries of a bank's "meeting the need for credit services", but loan dollars are a valuable measure of***

the depth of commitment of a bank's resources to community credit needs. In fact, the ANPR implicitly acknowledges this when discussing the retail lending "screen" which "would measure a bank's retail lending relative to its capacity to lend in an assessment area . . ." We urge the Board to *retain the current approach* that *balances* ratings performance based on the number of loans and the value of those loans. Without this balanced approach mega-lenders will easily earn high ratings based on large volumes of small loans that may well represent only a small commitment of bank resources. Focusing on the number of loans originated or purchased and excluding the value of those loans also would inure disproportionately to the benefit of the credit card lenders who extend large numbers of credit card accommodations that represent relatively small dollar amounts. CRA ratings should consider not only the reach of lending services into the community, but the commitment of a bank's resources too.

- We do like the use of quantitatively defined "comparators" that apply a specific numerical formula to the "community" (i.e., demographic) and "market" data (i.e., the aggregate lending reported by HMDA and CRA-reporting lenders). Since 1994 the demographic and "peer" or "aggregate" parameters have been identified but never quantified in either the Regulation, the Q&A's, or any guidance letters. The ANPR's proposal to adopt a 70% calculation applied to the market ("aggregate") comparators and a 65% factor to the "community" or demographic comparators is a simple but important step forward clarifying the thresholds necessary to attain a "satisfactory" or other performance rating. When we perform analysis for our bank clients, we have been comparing their penetration rates under the geographic and borrower characteristics tests for years. Our experience leads us to believe that the comparator factors of 70% and 65% for the market and community parameters are a bit high. We note the OCC adopted factors of 65% and 55% for the market and community parameters which our experience leads us to believe is more realistic.
- The ANPR suggests merging income categories (specifically, low- and moderate-income) and loan categories within a product line (e.g., all home mortgages) in the calculation of the presumptive satisfactory performance rating. Combining borrower income classes, tract income classes, and loan categories we believe is appropriate as proposed. Moreover, for most community banks, the loan volume is insufficient to develop statistically significant results when a high degree of granularity is applied. We believe more granular analysis is appropriate only when loan volume is sufficient to attain statistically meaningful results. We would suggest an absolute minimum volume of 50 loans per loan subcategory (low- and moderate-income borrowers, mortgages by purpose, etc.) should be used to determine when a more granular analysis is warranted and meaningful.

- The Board also proposes "to combine all years of the evaluation period together under a single metric calculation." **We see this last idea as unworkable.** During a 3- to 5-year evaluation period the income classification of census tracts may change. This will make for a confusing and complicated computation. Additionally, when the decennial census is put into effect, not only will tract income classes change; tract boundaries and tract identities also will change in many cases. We do, however, agree with merging LMI tracts and borrowers and loan subcategories into single computations for each. The granularity associated with present methodology we believe offers no significant advantage that would exceed the benefit of the Board's proposed merger of loan data (except the problems associated with the consolidation of multiple years as explained above).
- We suggest for the purposes of evaluating mortgage lending in LMI tracts that for multifamily units, the number of living units financed should be counted as an equivalent to the same number of single housing units. As proposed, a bank that finances a 100-unit apartment complex in an LMI tract would receive the same credit as a bank extending a single-family mortgage in that LMI tract (at least in the current regulation the size of the multifamily mortgage would be considered because loan values are part of the test). This vastly understates the value of the number of housing units financed in the apartment complex and creates a misleading comparison with single-family mortgages. Why should the proposed tests give a $100,000 single-family mortgage the same value (that is as 1 loan) as a $10 million loan that finances 100 living units in an AA LMI tract? We are not talking about multifamily affordable housing which would be valued at the outstanding mortgage balance for CD purposes. To be clear, we are simply referring to the geographic test that measures the penetration rate lending in AA LMI geographies.
- We suggest that *market rank and market share tables be incorporated into the standard tables* as an important part of performance context. The competitive structure of the market is an important performance context circumstance that should help put a bank's performance into perspective. For example, a residential mortgage market with significant lending by subprime lenders may skew the penetration rates lending to low- and moderate-income homeowners. Relying on just the borrower penetration rates extracted from the Aggregate data overlooks this important performance consideration. We would never analyze a bank's record of meeting the community's need for credit services without having market rank and share data available to provide much need insight into the competitive dynamics driving the market's LMI borrower penetration rates for example.

✓ **<u>Community Development activity</u>**:

- We approve of the idea of evaluating CD loans and CD investments based on outstanding balances, although we recommend reporting these items as distinct categories since the characteristics of loans and investments are quite different.
- We recommend **geocoding CD loans and investments** to the tract level. There is a drastic shortage of public information pertaining to CD activity. It is almost impossible to assess the "need" for community development activity when almost nothing is reported and the little data that is reported contains not an iota of location details. We strongly recommend reporting the activity by tract and by lender. <u>*Every lender that has financed public good projects touts those projects (site billboards for example) because such activity enhances the bank's market image*</u>. There should be no objection from the banking community to the dissemination of community development financing information that banks ordinarily like to publicize. Furthermore, the information will be invaluable for performance context considerations. *We also recommend including the CD purpose* fulfilled by reported CD lending and CD investing because it serves the public interest and will thereby provide much greater insight into community needs. Again, we anticipate little or no bank opposition to such disclosure.
- We suggest that *donations for a qualified CD purpose should have a multiplier applied that would equate the value of the donation to the value of an investment or loan outstanding for one year.* Many community banks fulfill their Community Development responsibilities by making donations rather than extending CD loans or CD investments. This puts community banks at a disadvantage if compared to benchmarks established by outstanding loans or investments by large banks. We suggest a multiplier of 50, meaning contributions of $20,000 would be the equivalent of $1 million of CD lending or investing for one year. This translates the cost of the money donated into the equivalent cost of an investment for 1 year.
- We encourage the Board to publish a list of acceptable proxies for affordable housing activities. It is relatively easy to determine if a rent is "affordable" for a low- or moderate-income tenant, but it is difficult to obtain specifics about the income of tenants in projects that do not have set aside provisions. We encourage the publication of proxy data that would be presumed as acceptable qualifiers in the absence of explicit tenant income information. In particular, we urge a proxy whereby if more than 50% of the families in a census tract are classified as low- or moderate-income families it would be presumed that more than half the tenants in an apartment complex would be qualified as low- or moderate-income tenants.
- Regarding Economic Development, we suggest the Board remove the size test because the goal of economic development is job creation, retention, or improvement. The

focus is on the beneficiary, so why should jobs created by larger companies not be considered as eligible for economic development consideration?

✓ **<u>Small Banks:</u>**

- We strongly suggest that the retail lending performance measurements be universal with respect to banks, no matter their size. The reality is that lending in the assessment area low- and moderate-income tracts, the "geographic" test, and the "borrower characteristics" test have been in practice for decades for banks of all sizes. What has been missing is the specific quantitative calculation of the comparators. The concept of applying 70% and 65% factors (or other percentages based on empirical data) would be enormously helpful and clarify what has been a very ambiguous part of performance ratings. Everyone has known the parameters, but without specific quantitative benchmarks, no one has known what the real standards have been. This not only has left a big gap in the transparency of performance ratings it also has left the door open for inconsistent application by examiners. The application of percentages to the benchmarks would be very simple and could be applied to data already collected to develop a base of empirical data that could help refine the benchmarks for different markets. There is really no need to make complicated and potentially confusing changes to the Regulation. Some simple "tweaks" of what has been in practice for more than a quarter of a century could really be transformative. The refinement of the comparator concept with specific quantitative calculations applied to lending activity would be enormously beneficial and help transform even the "qualitative approach used in the current examination procedures for small banks" to the true "metrics-based approach" the Board recognizes benefits everyone. Far from being turned off by this approach, small banks should find it very appealing because it will eliminate the vague and inconsistent interpretations from examiners in the field, who may have very differing subjective understandings and it will make performance ratings far more consistent and predictable.

✓ **<u>Timeliness of public data:</u>**

- A very troubling aspect of the annual Aggregate & Disclosure data is the very late publication of the data. For 2019 and 2020, the A&D files were not released until the week before Christmas in the following year. It is imperative that the important annual A&D files be released on a timelier basis, not later than June 30, of the following year. If the CFPB can publish HMDA-reported activity within 60 days of the March 1, annual deadline, why can't the FFIEC release the annual A&D files in a similar time frame?

Even more puzzling is the HMDA file structure went through dramatic changes in the past 3 years, whereas the CRA file structure has been the same for decades (and is a much smaller file too).

✓ **Business Demographics:**

- We call to your attention what we believe is unreliable and potentially misleading business demographic information that has been historically used for CRA purposes and likely will be the source for the "geographic peer comparator" and "demographic peer comparator" under the distribution tests applied to the "Small loan to business product line". We suggest the agency consider substituting the transparent public database published by the Bureau of the Census, the Census County Business Patterns database.
- We have compared the business demographic counts of businesses currently used by examiners in CRA evaluations to the count of businesses as published by the Census Bureau in its Census County Business Patterns database and its Statistics of US Business ("SUSB") and found extremely large disparities between the proprietary source data used by examiners currently and the Census Bureau files. Below we show a table that compares data for 3 New York counties extracted from the current source used by examiners and the Census Bureau data. The Census Bureau data is usually published 2 years after the date pertaining to the data. As of the date of these comments the latest data we have is 2018 for "firms" or "establishments" that employ workers and for non-employer businesses (self-employed people).

Table 1: Major Disparities between FFIEC Business Demographics and Census Bureau Business Demographics

	Dutchess County NY	Orange County NY	Ulster County NY
2018 Business Demographic used for CRA	**17,701**	**23,687**	**11,696**
2018 Census County Business Patterns:			
Establishments with employees	**7,607**	**9,596**	**4,850**
Non-Employer businesses	**22,767**	**26,842**	**16,953**
Total Firms and Non-Employer businesses	**30,374**	**36,438**	**21,803**

- The table reveals extremely large differences in the count of businesses between the Census Bureau data and the source used by examiners. It is not clear if the current source used by regulators includes self-employed businesses or not (although given the large disparity between the FFIEC business counts and the Census Bureau's "establishment" counts, it would appear that the FFIEC demographics include at least some non-employer entities), so we have included that information in the Census Bureau data in the table above. The discrepancies between the regulator database and the Census Bureau data are exceptionally large *with or without the non-employer businesses* and should call into question the reliability of the demographics used for two important CRA tests (geographic and borrower) under current CRA practices and proposed to be used in the ANPR. In 25 years of comparing the market-reported small business lending extracted from the A&D annual files we have never seen any situation in which the penetration rates lending to small businesses evidenced in the Aggregate data even came close the demographic standard used by examiners. This experience reinforces our skepticism about the reliability of the business demographic used by the examiners. We encourage the agency to reconsider the use of the business demographic database. Aside from its questionable accuracy, the data source is a proprietary product, and its use conveys a virtual monopoly on this important demographic.

- We also point out to the Board that the number of non-employer businesses dwarfs the number of "establishments" according to Census Bureau records (25.3 million compared to 7.9 million for the United States). There are important implications deriving from this fact. First, it is certain that almost all non-employer entities would have Gross Annual Revenues below the current $1 million GAR threshold measured in the "Borrower Characteristics" test for CRA exam (in fact, 99.84% are below the GAR threshold – see comments below). If the business demographics used by regulators include non-employers, then the sheer disparity in the number of non-employers compared with establishments would indicate that in virtually every market the relative percent of businesses with GAR<=$1 million will be 90% or more. But self-employed people (who may be part-time self-employed) are likely to rely on consumer types of loans such as HELOC's to finance their businesses (which are often at-home businesses). If this is true, it means banks may be financing many more businesses than official data suggests. Therefore, it is important to determine if the current business demographics file used for CRA purposes includes non-employers. It also is important to know if the current official file includes "shell corporations" used for real estate holding purposes. That too has important implications for the business demographic file. We suggest that the business loan market be divided into distinct segments that recognize the important differences between the business "establishments" sector of the business community and the non-employer segment. Given the sheer size of the non-employer market (81% of the business community according to an SBA study), breaking it out from the general business demographics would acknowledge the recognition that such a large segment of the business community warrants.

- A 2017 Census Bureau Report, "*Nonemployer Statistics by Demographics*", reveals that only 0.16% of the Nonemployer firms had Gross Annual Revenues >=$1 Million. In other words, 99.84% of Nonemployer businesses fall into the <=$1 million GAR category. That same data shows that nearly 41% of those firms had GAR <$10,000 and almost 65% had GAR <$25,000. Businesses that small are not likely to finance their business with traditional commercial financing.
- In fact, a 2018 study by the SBA indicates that 79% of non-employers rely on family savings to finance their businesses. Other important sources of capital are HELOCS, and credit cards. This means banks may be extending credit for businesses that does not appear in business loan data. This itself has dramatic implications for the "Borrower Characteristics" test administered in a CRA exam. ***If non-employers are included in business demographics, but their credit needs are fulfilled by consumer types of loans then regulators are comparing an inflated demographic with deflated borrowing data that do not include bank financing for the largest sector in the business market***. This means the business demographic used by the FFIEC is potentially seriously inaccurate and misleading.
- I can speak as someone who grew up in a small business family and who was named by the United States Small Business Administration as the leading banker advocate for small business in Connecticut when I was in banking. Now, I own my own small business. So, I urge the Board to step back and examine the reliability of the demographic data used to establish an important "Performance Context" community (demographic) factor and I urge the Board to conduct a study about how the financial needs of the dominant segment (non-employee businesses) of the business market are being met before it publishes a Notice of Proposed Rulemaking for CRA purposes later this year. If HELOCS and consumer credit cards are an important source of such small business financing, they are certainly not included in the CRA-reported small business financing.

✓ **<u>Reconsider serious data omissions Small business lending, certain Residential Mortgages and certain Community Development loans:</u>**

- The agencies historically have counted loans originated, refinanced, and renewed subject to a once-per-year limit of any loan. *We have observed what we* *believe to be a serious shortcoming in the definition of what constitutes a "renewal" for CRA purposes*. Specifically, the Regulation recognizes a renewed loan when the underlying maturity of the loan is extended by the lender. The problem with this approach is that many revolving lines of credit that are renewed annually do not meet this definition and are therefore excluded from being reported. The technicality that disqualifies these loans is that they are typically secured by UCC filings and the underlying notes are callable on demand. Therefore, the annual renewals do not extend the maturity of the note and are not qualified as "renewals" under the CRA definition. The reason demand notes are used to evidence debt is to avoid interrupting the "perfection" of the continuity of the security interest of the lender. If a new note were to be issued upon each annual renewal the new note would constitute the start of a new security interest and any intervening liens would supersede the security interest of the lender. This is a question of safety and soundness. Consequently, many revolving lines of credit go unreported for CRA purposes. This has 2 very undesirable CRA consequences. First, it results in underreporting the small business lending activity of lenders extending secured revolving lines of credit, thereby denying those lenders the recognition they deserve for extending small business credit accommodations (and one that qualifies as flexible, complex, and innovative too). Second, aside from affecting individual lenders the omission of secured revolving lines of credit could result in significant underreporting of the true small business loan market if enough lenders are extending these types of credit facilities to the business community. If the CRA is all about, "meeting the need for credit services", what better indicator of that need is there than the reported actual lending activity? But if a significant sector of the loan market is disqualified from being reported for a technical reason, that means the best indicator of the need for small business credit is potentially significantly understated. I have seen much anecdotal evidence indicating that secured revolving lines of credit are a significant segment of lending to the business community. <u>*Therefore, we urge the Board to reconsider the definition of a "renewal" for CRA purposes*</u>. The OCC in its 2020 final rule does include the broader definition of "renewals" for CRA purposes.

- As the Board is aware, under the current Regulation C, certain dwelling-secured mortgages whose proceeds are used for a business purpose are not reportable (if they are not for a home purchase, refinance or home improvement purpose). Regulation BB disqualifies the reporting of dwelling-secured loans that are extended for a business purpose unless the mortgage is taken as "an abundance of caution." The underlying reason for not reporting business purpose loans secured by a dwelling is that such loans historically would have involved double-reporting and/or double-counting such loans for both HMDA and CRA purposes. But now business purpose loans secured by a dwelling are not "covered" under HMDA unless they are for the purpose of purchasing, refinancing or improving a dwelling. This means the historical reason for disqualifying small business loans secured by a dwelling are no longer applicable for dwelling-secured loans not "covered" by Reg. C. We respectfully suggest that the Board therefore, reconsider the prohibition of reporting business loans secured by residential property as long as such loans are not "covered" by HMDA. This could result in a significant increase in the volume of reported small business loans since it is a common practice in commercial lending to secure loans to closely held businesses with the principal residence of the business owner(s).

- Regarding activity regarded as Community Development activity under the "Economic Development" definition, we strongly recommend the Board consider revising the "Economic Development" qualifications in 2 ways: (1) allow "job creation, preservation, or improvement" to include jobs without applying the "size" test and (2) small business loans that have job creation qualifications should be reported as small business loans *and* as community development loans.
    - ❖ Jobs for low- and moderate-income persons are valuable to those people no matter who the employer or size of the business. So why apply a "size" test that disqualifies many job-creating loans created by larger businesses? One of the primary goals of the CRA is to encourage banks to support the LMI community. Therefore, any financing that improves permanent employment within the LMI community ought to be considered under the "Economic Development" definition. Disqualifying loans solely because the jobs are created by a large company makes no sense. Any activity that supports permanent jobs for LMI persons ought to be credited as qualified as economic development.
    - ❖ We also encourage the Board to allow recognition of job creation, preservation, or improvement when a loan extended as a "small business loan" also has qualified permanent job activity. There is no doubt that many loans extended to small businesses also involve jobs-related activity, but all such loans are reported as small business loans and not considered as community development loans except when a bank is being examined under Intermediate-Small Bank examination standards, during which an ISB can elect on a loan-by-loan basis whether to have a small business loan counted under the "Lending Test" or the "Community

Development Test". We urge the Board to reconsider this policy and to allow for "small business loans" that also have qualifications as "community development" under the "economic development" definition to be considered as qualified for both purposes. Once again, any lending that supports permanent jobs for LMI persons should be recognized as community development and not disqualified as such because the loan also is qualified as a "small business loan". Therefore, we suggest the Board allow recognition for such loans to be qualified as both small business loans and community development loans or, the Board should apply the current elective to all bank under all examination standards.

✓ **An Expanded List of Qualified Activities:**

- We endorse the publication of an expanded, but not exhaustive, list of qualified community development activities which we believe is highly desirable and will help address ambiguous situations banks often encounter. In particular, we have observed numerous situations involving multifamily affordable housing that did not have a formal set aside agreement and were denied credit because of lack of information about tenant income. There should be a proxy, such as a family income demographic showing more than 50% of the families in the census tract where the multifamily affordable housing is located are LMI families.

Sincerely,

Len Suzio

Leonard F. Suzio Jr., President

GEODATAVISION "WE MAKE DATA WORK FOR YOU"

Compliance Tools for Compliance Professionals

Synopsis: We believe most of the laudable goals in the ANPR can be accomplished without dramatic changes. Small changes can make a big difference. Minor modifications to the current tests and data types can create a more refined and accurate system of measuring performance that can be highly effective and achieve the goals of the ANPR. These minimal "tweaks" can be complemented by only a small number of significant changes.

- **Loan volume adequacy Tests**
  - ✓ Maintain the 50% threshold but,
  - ✓ If lending <50% within AA's, then compare to loan-to-deposit data reported in market with an adjustment for difference between Mortgages-to-Deposits and Loans-to-Deposits (GDV has a model that computes this difference). Compare expected loan volume (based on market relationship of loans to deposits) to actual loan volume.
  - ✓ Determine if more than 50% of adjusted domestic deposits are from outside the AA and if so, mandate deposit-based assessment areas but with performance standards that are modified to reflect the competitive disadvantages of not having facilities nor personnel in deposit-based communities.
- **Lending Gaps Analysis** (now that loan volume is adequate, how is it dispersed throughout the community)
  - ✓ Maintain the current "conspicuous gaps in contiguous tracts" model that determines if there are unexplained geographic lending gaps in the community.
- **Lending in AA LMI Geographies ("Geographic Test")**
  - ✓ Maintain the current "penetration rate" analysis using specific "comparators" based on the "market" (loan market LMI tract penetration rates) and "community" (demographic – distribution of OOHU and businesses by AA Tract Income Class) parameters. Market comparators of 70% and community comparators of 65% may be a bit high. Calculations should be based on a balanced approach using both loan counts (originations, purchases, and renewals) and loan values. Retaining dollar-based measurements is important to measuring true bank commitment to CRA in light of its size and resources.
- **Lending based on Borrower Characteristics Test.**
  - ✓ Maintain the current "penetration rate" analysis using specific "comparators" based on the "market" (mortgage market LMI borrower lending penetration rates and very small business borrower lending penetration rates) and "community" (demographic) parameters. Market comparators of 70% and community comparators of 65% may be a bit high. Calculations should be based on a balanced approach using both loan counts (originations, purchases, and renewals) and loan values.

- **<u>Community Development Test</u>**
  - ✓ Compare outstanding AA CD loan balances to AA deposits with a specific "comparator" TBD (relative to AA deposits or, ideally to the reported CD loans outstanding should the Board mandate the collection and reporting of that information).
  - ✓ Compare outstanding AA Investment balances to AA deposits with a specific "comparator" TBD (relative to AA deposits or, ideally to the reported CD investments outstanding should the Board mandate the collection and reporting of that information).
  - ✓ The Board should mandate the collection, purpose, and geocoding (to the tract level) and reporting of CD lending and investments. This information is badly needed to develop a picture of the CD needs of a community. Currently, only CD loans are reported but without location. This leaves an enormous information vacuum regarding the CD market. The Board may be reluctant to mandate the reporting of such activity which the Board may believe banks will be reluctant to have publicly disclosed. However, our experience indicates the exact opposite is true. Banks normally publicize their CD activities posting big signs at sites where they have financed affordable housing, or economic development projects or where they have funded vital community services (health clinics for example) or where they have supported economic development or revitalization activities. We believe there will be little, if any resistance, to the idea of collecting and disclosing this information other than some banks may regard it as added regulatory burden. This information is too important to everyone, (examiners, community leaders, and bankers themselves) for it not to be reported!
  - ✓ A multiplier should be applied to qualified CD donations that would equate the value of a donation to the value of an investment. We suggest a multiplier of 40 to 50 times the contribution amount to arrive at an equivalent traditional investment amount for any given year. Without this multiplier, the value (and cost) of qualified donations will be substantially understated relative to true investments. Our experience indicates that community banks frequently rely on qualified donations to count toward their CD investment performance. Since the Board proposes a benchmark relative to AA deposits outstanding it will be imperative to adjust the value of CD donations to an equivalent outstanding investment, otherwise community banks subject to the Community Development test will be significantly handicapped meeting this test.
  - ✓ Compile CD services based on all bank employee volunteer hours without requirement for volunteer activity to be financial in nature or related to the expertise of the volunteer. Comparator number of hours based on number of

bank employees could be developed. For example, target 4 volunteer hours average per employee per year. A bank with 100 employees would have a benchmark of 400 volunteer hours annually.

- ✓ All banks with more than $300 million but with $1 billion or less of assets could be subject to a Community Development Test based on qualified CD contributions. The Test would be benchmarked relative to a bank's profitability, say 1% of net pretax profits for example.

- **Assessment Area Delineation:**
  - ✓ The flexibility in the current rule that allows a bank to modify its Assessment Area to the market "it can reasonably be expected to serve". It is extremely important to preserve this flexibility because if banks are coerced into delineating unrealistically large AA's the performance standards themselves will be unrealistic and result in misleading conclusions about bank performance. Our review of the 2020 annual SOD data and the 9/30/2020 FDIC SDI data indicate there are a significant (623) number of banks with more than $1 billion of assets but with 5 or fewer branches. Among our own clients we have identified a number of banks with more than $1 billion of assets but with Assessment Areas that include parts of counties in which those banks have only 1 branch. Compelling banks that small to annex entire counties would have a profound impact and consequences adverse to the goals of the ANPR.
  - ✓ Deposit-based Assessment Areas: We believe this will impact an extremely small number of banks but will compel all banks to geocode their all their domestic deposits. GeoDataVision currently is conducting a study of banks to determine the geographic dispersion of depositors relative to their Assessment Areas and their branch networks. Early results indicate that community banks generate only a relatively small percentage of deposits outside their defined communities. So far, the largest percentage of deposits outside a bank's Assessment Area(s) has been about 32%, far below the 50% trigger threshold for a "deposit-based Assessment Area in the ANPR. We would be pleased to make the results of our Deposit Dispersion Study available to the Board if it so desires. Please contact me if the Board is interested.
  - ✓ Our experience indicates a growing number of banks who run afoul of the AA Ratio test because those banks are engaged in mortgage lending and small business lending activities that use LPO's, brokers, and other means to develop volume beyond the traditional assessment areas. These banks fund these loans largely from sales into the secondary markets. Therefore, those banks use local deposits only as a temporary funding vehicle. We did not observe in the ANPR anything to address these situations. We suggest that the traditional AA rules be

retained but that loans extended outside a bank's AA be adjusted to reflect their net value after sale into the secondary market.

- ✓ If the Board mandates deposit-based AA's we suggest the performance standards be adjusted to reflect that an institution with no facilities and no personnel in a deposit-based market will be at a significant disadvantage competing with "hometown" banks that know their communities far better.

- **<u>Reporting</u>**:
  - ✓ All banks >$300 million asset size that are required to perform under CRA should be required to report under CRA. This is important because there is no true "peer" data available since only "large" banks report under the Regulation. There is little cost since a bank can download and use the free FFIEC software for reporting CRA activity. Most small banks generate a small volume of loans which means the data entry time and costs are minimal. One widespread handicap for small banks under CRA is that many banks do not collect their data and consequently go in to CRA exams blind. Examiners are compelled to conduct a "scientific" sampling which means more time and cost, and no one really knows how accurately the sampling reflects a bank's CRA performance. The minimal added costs are worth the tradeoff with benefits available to small banks. If the Board is willing to mandate the geocoding of thousands of deposits, even for non-reporting small banks (as has the OCC), why would it not be receptive to the far less onerous requirement to mandate the collection and report the lending activity of only 100 loans or so?

- **<u>Reconsider how certain types of loans are recognized or disqualified under CRA.</u>**
  - ✓ The definition of a "**renewal**" should be expanded to include the annual renewal of lines of credit evidenced by a demand note. The use of demand notes is common practice when UCC-secured lines of credit are extended by banks and the current policy disqualifies all these loans from recognition as small business loans.
  - ✓ Allow the *reporting of small business loans secured by lien on a dwelling*-secured property if the loan is for a business purpose and the loan is *not reported under HMDA*.
  - ✓ Recognize all loans that support permanent job creation, preservation, or improvement to LMI persons as "economic development" without requiring a "size test" and without disqualification of a loan because it also qualifies as a small business loan.

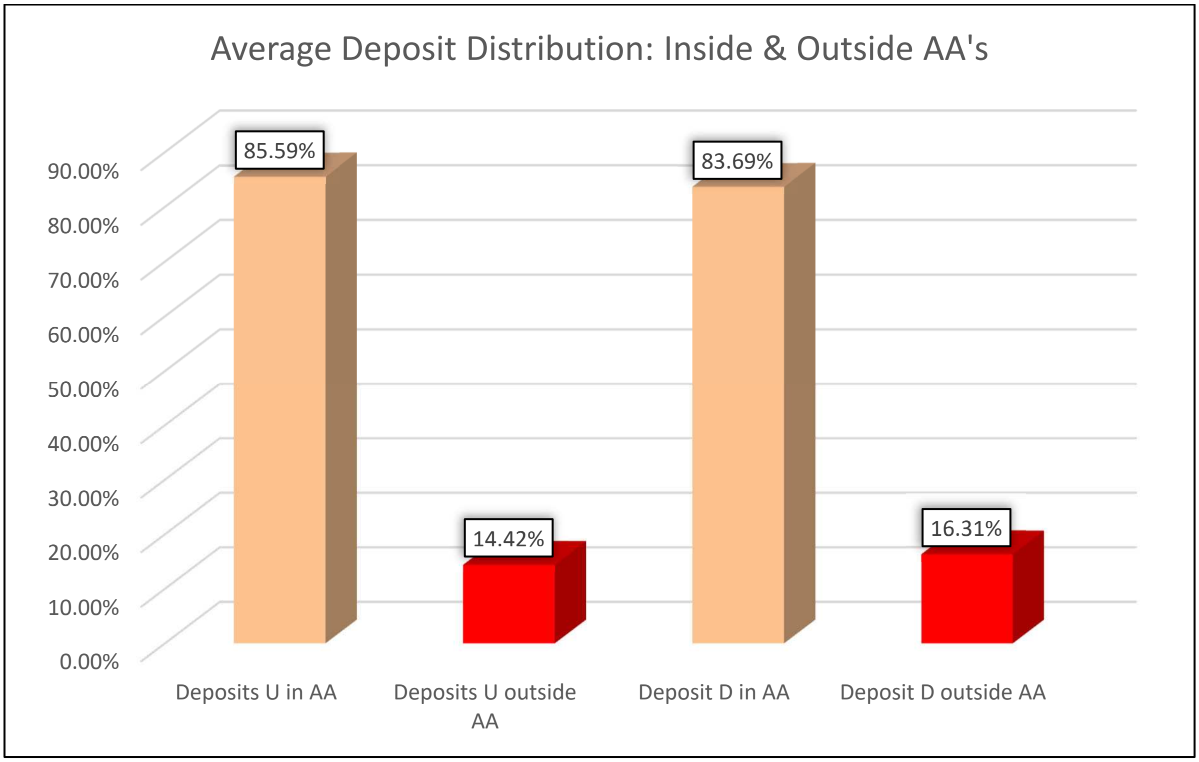
GeoDataVision Community Bank Geographic Deposit Dispersion Study

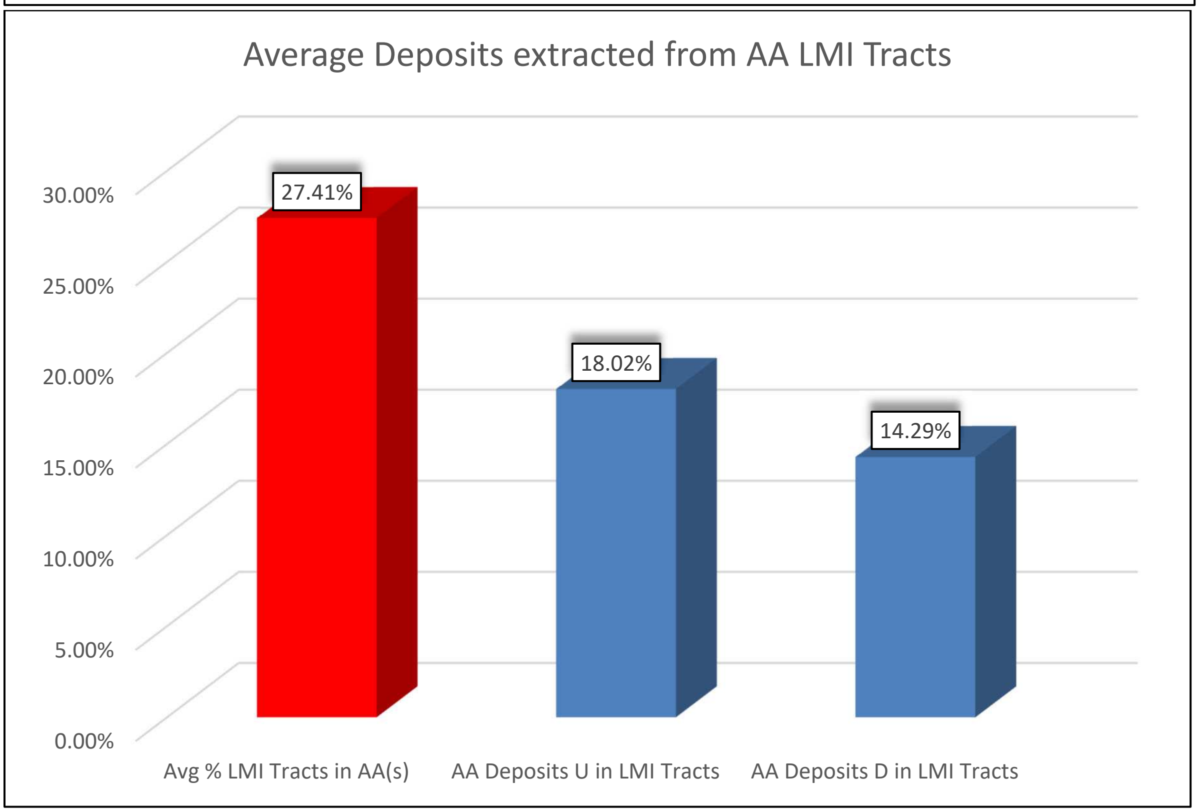
GeoDataVision is working with several dozen banks (final number yet to be determined) to map the geographic dispersion of their deposit accounts. The Study will include:

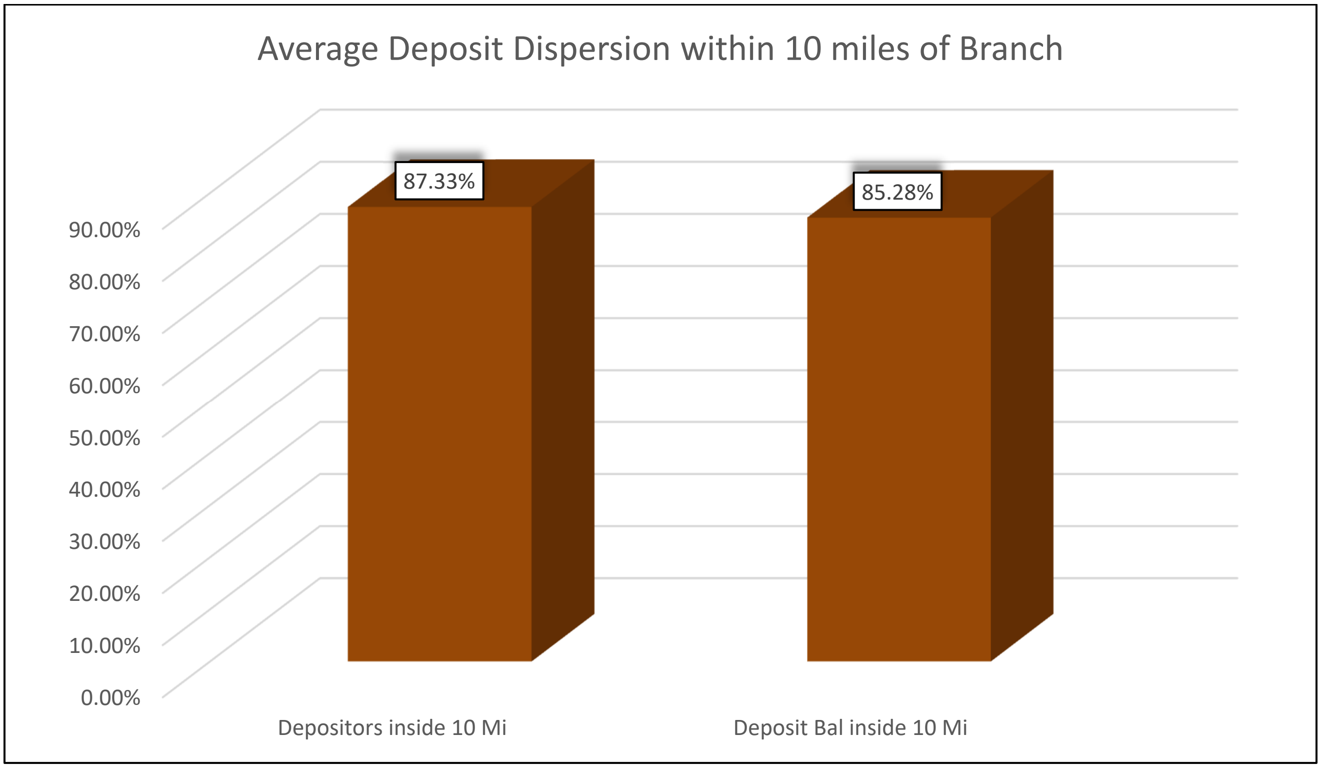
- ✓ Computation of the relative number of deposits inside versus outside a bank's assessment area(s)
- ✓ Computation of the relative volume ($) of deposits inside versus outside a bank's assessment area(s)
- ✓ Computation of the count and relative volume ($) of deposits within 10 miles of a bank's branch system
- ✓ Determination of the relative count and volume ($) of assessment area(s) deposits within assessment area(s) LMI tracts compared to all deposits in assessment area(s)
- ✓ Determination of the relative count and volume ($) of deposits attracted from outside assessment area(s) LMI tracts relative to all deposits captured from outside assessment area(s)
- ✓ Participating banks currently range from $362 million in deposits to $1.1 billion of deposits with an average of $822 million domestic deposit balances outstanding

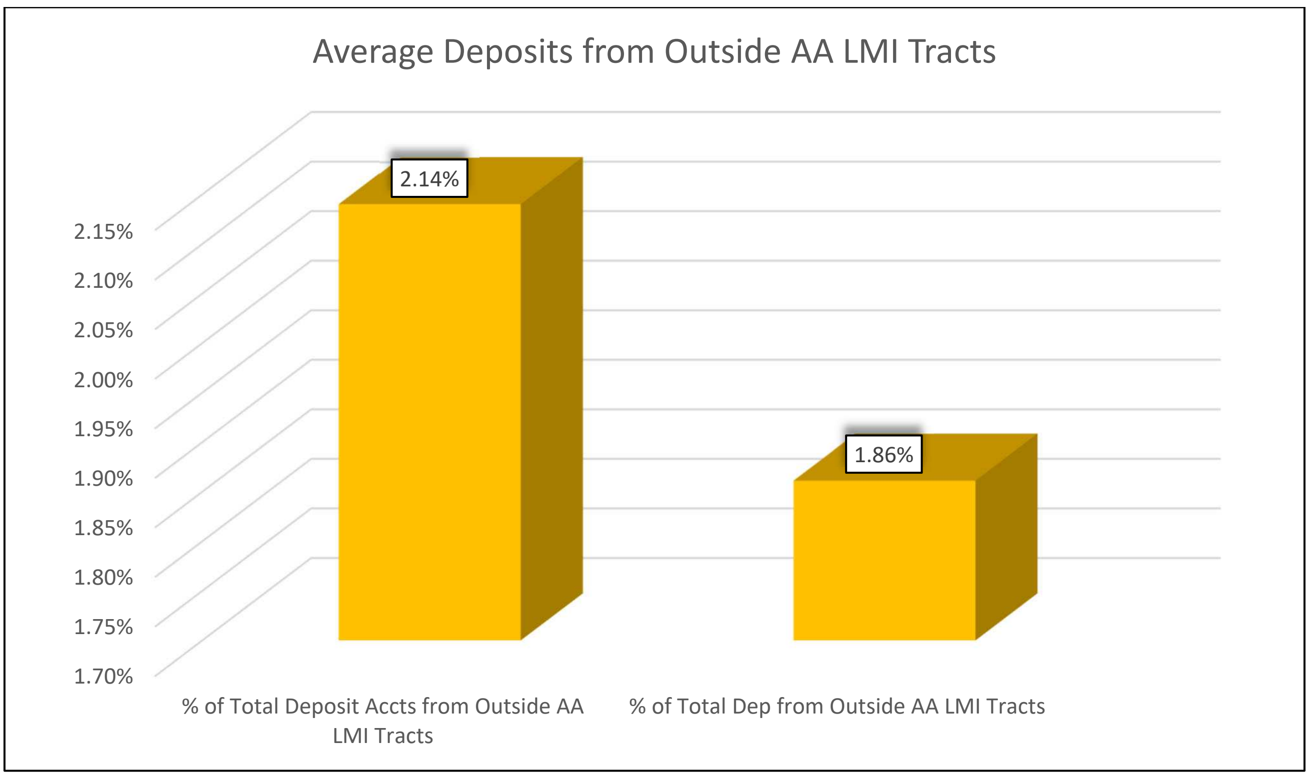
As of 2/16/2021:

- ✓ The highest volume of *deposits attracted from outside any bank's assessment area* 24.7% when computed based on deposit counts and 32.7% when calculated based on deposit balances. On average, 16.3% of deposit balances were attracted from outside assessment area(s)
- ✓ When computed relative to a branch network regardless of assessment area boundaries, the Study thus far indicates that an average of *85.6% of depositors and 83.7% of their deposits were located within 10 miles of the nearest bank branch*
- ✓ Deposits attracted from within assessment area LMI tracts: on average 27.4% of tracts within assessment areas were LMI tracts. In comparison, 18.0% of depositors and 14.3% of deposit balances were extracted from AA LMI tracts.
- ✓ Deposits attracted from LMI tracts outside assessment areas: on average 14.8% of depositors and 10.7% of deposit balances from outside assessment areas were captured from LMI tracts outside assessment area(s). In other words, when computed relative to total deposits on average only 1.9% deposit balances were taken from LMI tracts outside the assessment areas


Average Deposit Distribution: Inside & Outside AA's
90.00%
80.00%
70.00%
60.00%
50.00%
40.00%
30.00%
20.00%
10.00%
0.00%
85.59%
14.42%
83.69%
16.31%
Deposits U in AA
Deposits U outside AA
Deposit D in AA
Deposit D outside AA


Average Deposits extracted from AA LMI Tracts
30.00%
25.00%
20.00%
15.00%
10.00%
5.00%
0.00%
27.41%
18.02%
14.29%
Avg % LMI Tracts in AA(s)
AA Deposits U in LMI Tracts
AA Deposits D in LMI Tracts


Average Deposit Dispersion within 10 miles of Branch
90.00%
80.00%
70.00%
60.00%
50.00%
40.00%
30.00%
20.00%
10.00%
0.00%
87.33%
85.28%
Depositors inside 10 Mi
Deposit Bal inside 10 Mi


Average Deposits from Outside AA LMI Tracts
2.15%
2.10%
2.05%
2.00%
1.95%
1.90%
1.85%
1.80%
1.75%
1.70%
2.14%
1.86%
% of Total Deposit Accts from Outside AA LMI Tracts
% of Total Dep from Outside AA LMI Tracts