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**Re: Community Reinvestment Act; Interagency Questions and Answers¹
OCC (Docket ID OCC-2013-0003)
Board (Docket No. OP-1456)
FDIC**

¹ See 78 Fed. Reg. 16765 (March 18, 2013)

Dear Sir or Madam:

Capital One Financial Corporation (“Capital One”)² commends the Office of the Comptroller of the Currency, Federal Reserve Board, and Federal Deposit Insurance Corporation (collectively, “Agencies”) for taking on the task of holistically looking for ways to improve the implementation of the Community Reinvestment Act (CRA), and for giving careful consideration to industry and public comments provided in 2010. We appreciate the opportunity to provide comments on key aspects of this important area of banking regulation.

The CRA has been very effective in encouraging banks to serve low- and moderate-income (LMI) neighborhoods and individuals. We believe that most of the proposed changes will enable banks to achieve even stronger results, and thus help ensure that CRA remains a well-respected and sustainable law.

We have commented on many of the proposed changes. Our key points are as follows:

- Community development (CD) activities in statewide and regional areas, along with investments in nationwide funds, must receive full consideration in the evaluation process. Assurance that such activities will not be diminished or “discounted” will encourage banks to distribute capital to underserved markets in broader statewide or regional areas that include their Assessment Areas.
- The regulation should not make CD lending a required activity. Many banks do not have the necessary expertise or infrastructure to make complex CD loans, which could have the unintended effect of destabilizing this market. If such banks believe they *must* originate specialized types of CD loans, a consequence may be a significant increase in such lending without a full understanding of how to structure these transactions with adequate credit risk parameters and appropriate pricing. CRA should encourage and allow banks to focus on what they do best (within the context of prudent practices) and therefore have the greatest potential impact on their communities; it should not require every bank to be engaged in all types of CRA activities. Requiring all banks to engage in CD lending would also increase competition to unhealthy levels and lead to riskier lending practices and

² Capital One Financial Corporation (<http://www.capitalone.com>) is a financial holding company whose subsidiaries, which include Capital One, N.A. and Capital One Bank (USA), N. A., had \$212.4 billion in deposits and \$300.2 billion in total assets as of March 31, 2013. Headquartered in McLean, Virginia, Capital One offers a broad spectrum of financial products and services to consumers, small businesses and commercial clients through a variety of channels. Capital One, N.A. has more than 900 branch locations primarily in New York, New Jersey, Texas, Louisiana, Maryland, Virginia, and the District of Columbia. A Fortune 500 company, Capital One trades on the New York Stock Exchange under the symbol "COF" and is included in the S&P 100 index.

unsustainably low prices as we have seen in current CRA “hot spots” (markets with intense CRA competition).

Our full comments are presented below.

Proposed Revisions to Existing Q&As

I. Community Development Activities Outside an Institution's Assessment Area(s) in the Broader Statewide or Regional Area That Includes the Institution's Assessment Area(s)

§ __.12(h)—6: Must there be some immediate or direct benefit to the institution's assessment area(s) to satisfy the regulations' requirement that qualified investments and community development loans or services benefit an institution's assessment area(s) or a broader statewide or regional area that includes the institution's assessment area(s)?

A6. No. The regulations recognize that community development organizations and programs are efficient and effective ways for institutions to promote community development. These organizations and programs often operate on a statewide or even multistate basis. Therefore, an institution's activity is considered a community development loan or service or a qualified investment if it supports an organization or activity that covers an area that is larger than, but includes, the institution's assessment area(s). The institution's assessment area(s) need not receive an immediate or direct benefit from the institution's participation in the organization or activity, provided that the purpose, mandate, or function of the organization or activity includes serving geographies or individuals located within the institution's assessment area(s).

In addition, a retail institution will receive consideration for certain other community development activities. These activities must benefit geographies or individuals located somewhere within a broader statewide or regional area that includes the institution's assessment area(s). Examiners will consider these activities even if they will not benefit the institution's assessment area(s). However, such community development activities must be performed in a safe and sound manner consistent with the institution's capacity to oversee those activities and may not be conducted in lieu of, or to the detriment of, activities in the institution's assessment area(s). When evaluating whether community development activities are being conducted in lieu of, or to the detriment of, activities in the institution's assessment area(s), examiners will consider an institution's performance context, including the community development needs and opportunities in its assessment area(s), its business capacity and focus, and its past performance.

§ __.12(h)-7: What is meant by the term, “regional area”?

A7. A “regional area” may be an intrastate area or a multistate area that includes the financial institution's assessment area(s). Regional areas typically have some geographic, demographic, and/or economic interdependencies and may conform to commonly accepted delineations, such as “the tri-county area” or the “mid-Atlantic states.” Regions are often

defined by the geographic scope and specific purpose of a community development organization or initiative.

We agree that these two Q&As could benefit from clearer guidance. We also agree that partnerships (e.g. loan pools, investment funds, volunteer services) with community development organizations and programs are efficient and effective ways for institutions to promote community development. This type of pooled-interest partnership provides opportunities for institutions that do not have the capacity to engage in these activities alone. Risks are also shared by all the participants, a compelling argument especially useful when engaging in activities that are higher risk. Often these organizations and programs operate on a statewide or regional basis. Therefore, we support the proposed clarification that “an institution's activity is considered a community development loan or service or a qualified investment if it supports an organization or activity that covers an area that is larger than, but includes, the institution's assessment area(s).”

We also support the Agencies' attempt to ensure that statewide and regional activities receive full consideration in the evaluation process and the related elimination of any standards tying such consideration to the immediate or direct benefit of an assessment area. Given that specific locations are not always available at the time of participation in many statewide or regional loan pools and investment funds, we agree with the position of the Agencies that the standard cannot be based on immediate or direct benefit to the institution's assessment area(s).

Proper clarity in these Q&As will achieve two important objectives ultimately benefiting LMI populations and areas. First, with full assurance that statewide and regional CD activities will not be discounted or diminished in any manner, banks will be more likely to participate in such activities. And second, more CD activities are likely to occur in underserved markets and competition may be reduced in “hot spot” markets that are experiencing unsustainably low pricing and acceptance of greater credit risk due to unhealthy levels of CRA competition.

- *Do the revised Q&As clearly convey the Agencies' intent that community development activities in the broader statewide or regional area that includes an institution's assessment area(s) will receive consideration?*

For the most part, the proposed language appropriately conveys the Agencies' intent that these types of CD activities should receive consideration. However, the Agencies should be very clear in the guidance that CD activities in statewide or regional areas also receive the same level of consideration, quantitative as well as qualitative, as activities in the assessment area itself. The basis for such consideration would be both the activity and the bank's assessment area being within the same statewide or regional area.

- *Will this clarification of consideration in the broader statewide or regional area that includes an institution's assessment area(s) provide an incentive for banks to increase their community development activities or expand their opportunities to engage in community development activities?*

Yes, as long as there is assurance of full quantitative and qualitative consideration. Statewide and regional activities need to be fully allocated to assessment areas to ensure full consideration. The method of allocation should not require a specific formula nor be prescribed in any fashion that might deter the decision to make the investment. Rather, a bank's method of allocation should be accepted as long as reasonable.

- *Does "community development activities being conducted in lieu of, or to the detriment of, activities in the institution's assessment area(s)" raise the same uncertainty as "adequately addressed the community development needs of its assessment area(s)"? If so, how can the Agencies better describe the concept that a financial institution cannot ignore legitimate and financially reasonable community development needs and opportunities in its assessment area(s) to engage in community development activities elsewhere in the broader statewide or regional area when those activities will not provide any benefit to its assessment area(s)?*

The newly proposed language may be even more problematic than the original language. Although we believe that both the current and proposed language lack sufficient clarity, the revised language could be interpreted as a higher bar than "adequately addressing" the needs. Strong arguments could be made that any activity outside the bank's assessment areas may have been done "in lieu of" or "to the detriment of" the assessment areas. If either standard of "in lieu of" or "to the detriment of" is adopted, further clarification will be needed as to how these standards would be met. A determination based on level of activity seems infeasible given the wide variances from one assessment area to another and erratic levels of opportunity year-to-year. Further, if the guidance is not clear enough for the bank to know without question at the time of the activity whether it will receive full consideration for statewide and regional activities, the revised Q&A will have failed to have solved the issue of certainty.

We propose instead that the guidance be clear by establishing a bright line. An effective bright line would be the most recent CRA rating. Any bank with an overall rating of Satisfactory or higher on its last examination would be automatically eligible to have statewide or regional CD activities fully considered in its next examination. This guidance would provide the certainty needed for banks to have complete assurance of full consideration of activities in the broader statewide and regional area. For banks with less than an overall Satisfactory rating, a more subjective analysis would be required including performance context, needs and opportunities in the bank's assessment area(s), and the bank's capacity and business strategies.

- *Does removal of the portion of current Q&A § __.12(h)-7 that discussed a diffuse potential benefit to an institution's assessment area(s) alleviate the confusion between the two Q&As and help to clarify that community development activities in the broader statewide or regional area that includes an institution's assessment area(s) will receive consideration?*

Yes. We support the Agencies' proposal to remove this language in an effort to eliminate ambiguities in the guidance.

- *Is the proposed definition of "regional area" sufficiently clear and appropriately flexible?*

Yes. The proposed definition of "regional area" is comprehensive enough to provide sufficient clarity and encompass all likely variations of geographic areas for inclusion.

II. Investments in Nationwide Funds

§ __.23(a)-2: *In order to receive CRA consideration, what information may an institution provide that would demonstrate that an investment in a nationwide fund with a primary purpose of community development will directly or indirectly benefit one or more of the institution's assessment area(s) or a broader statewide or regional area that includes the institution's assessment area(s)?*

A2. There may be several ways to demonstrate that the institution's investment in a nationwide fund meets the geographic requirements, and the agencies will employ appropriate flexibility in this regard in reviewing information the institution provides that reasonably supports this determination.

In making this determination, the agencies will consider any information provided by a financial institution that reasonably demonstrates that the purpose, mandate, or function of the fund includes serving geographies or individuals located within the institution's assessment area(s) or a broader statewide or regional area that includes the institution's assessment area(s). Typically, information about where a fund's investments are expected to be made or targeted will be found in the fund's prospectus, or other documents provided by the fund prior to or at the time of the institution's investment, and the institution, at its option, may provide such documentation in connection with its CRA evaluation.

Nationwide funds are important sources of investments for low- and moderate-income and underserved communities throughout the country and can be an efficient vehicle for institutions in making qualified investments that help meet community development needs. Nationwide funds may be suitable investment opportunities, particularly for large financial institutions with a nationwide branch footprint or for other financial institutions with a nationwide business focus, including wholesale or limited purpose institutions. Other financial institutions may find such funds to be efficient investment vehicles to help meet community development needs in their assessment area(s) or the broader statewide or regional area that includes their assessment area(s). Prior to investing in such a fund, an institution should consider reviewing the fund's investment record to see if it is generally consistent with the institution's investment goals and the geographic considerations in the regulations. Any investments in nationwide funds must be performed in a safe and sound manner, consistent with an institution's capacity to oversee those activities, and may not be conducted in lieu of, or to the detriment of, activities in the institution's assessment area(s).

When evaluating whether community development activities are being conducted in lieu of, or to the detriment of, activities in the institution's assessment area(s), examiners will consider an institution's performance context, including the community development needs and opportunities in its assessment area(s), its business capacity and focus, and its past performance. See also Q&As § __.12(h)-6 and § __12(h)-7 (additional information about recognition of investments benefiting an area outside an institution's assessment area(s).)

The Agencies intend for this proposed revised Q&A to apply only to nationwide funds. Institutions that are considering investments in statewide or regional funds would continue to rely on Q&As § __.12(h)-6 and § __.12(h)-7.

We agree that guidance regarding nationwide investments needs further clarification. We also agree that, similar to statewide and regional funds, nationwide funds provide benefits to promote community development such as being an efficient delivery channel of capital, spreading risks amongst numerous participants, creating opportunity for higher degrees of complexity and innovation, and distributing capital to underserved markets based on need rather than assessment area constraints.

To ensure the success of changes to the proposed guidance, institutions need certainty that these types of qualified investments will receive full consideration. As the case with statewide and regional activities, we would recommend that the phrases "in lieu of" or "to the detriment of" be deleted because of the level of ambiguity. We believe that the best way to ensure the necessary assurance for nationwide investments is to establish the previous overall CRA rating as the bright line. The institution would automatically be eligible for consideration of nationwide investments as long as it maintains an overall rating of Satisfactory or higher.

Full consideration also means that every dollar invested needs to be attributed to an assessment area of the institution. We recommend allocating investment dollars in assessment areas included in the same statewide or regional area where the fund plans to make investments based on the prospectus. The allocation should be determined by the bank and be reasonable. For example, the funds could be divided between assessment areas on the basis of the institution's deposits or branches in instances where there is more than one assessment area within that regional or statewide area.

Again, sufficient clarity will be required to ensure increased investment in nationwide funds. Therefore, institutions will need to have full assurance that the amount and qualitative impact of these investments will not be diminished in any fashion during the evaluation process. Achieving this level of certainty will encourage more investments in such vehicles resulting in broader geographic distribution of CD activities.

- *Would the proposed revised Q&A assist institutions that deliver products on a nationwide basis to address community needs in areas where they provide products and services?*

We continue to support the current guidance for institutions designated as wholesale or limited purpose to receive full consideration for investing or lending in nationwide funds under the community development test. However, for large retail banks where assessment areas are delineated by physical deposit-taking facilities, there still needs to be a link between the geographies where the investments are made and the bank's assessment areas. Using the same statewide or regional rules outlined in our response to the next question could easily apply here as well, with greater likelihood of overlap due to the broader coverage of assessment areas for the very largest retail institutions.

- *When might nationwide funds be appropriate investments for regional or smaller institutions?*

Regional or smaller institutions should have the same ability to receive consideration for investments in nationwide funds. Allocation of the bank's investments can be made on the basis of a statewide or regional area which includes the assessment area(s) of the bank and where, based on the prospectus, the fund plans to invest. Using a reasonable methodology, the bank would distribute the investments within those assessment areas.

- *Some commenters indicated that current methods of "earmarking" investments, including through the use of side letters, are burdensome. Are such methods, in fact, burdensome and, if so, in what way?*

Earmarking investments through the use of side letters is a burden to the fund syndicator because it must find properties that align with investor needs. However, we recommend maintaining the use of side letters as an option for the bank. If in practice the new proposals are more effective in encouraging investments and are less burdensome, banks will opt not to use side letters. If the revised Q&A does not work in practice and side letters have been eliminated as an option, there could be a severe decline in the volume of CD investing.

- *If the proposed revised Q&A is adopted, how should investments in nationwide funds be considered in an investing institution's CRA evaluation? Should there be a special category for investments in nationwide funds? How would such a category affect the amounts of an institution's investments at the assessment area and/or statewide levels?*

No, there should not be a special category. The exam methodology is already very complicated for banks that are likely to take advantage of nationwide investment opportunities. The objective should be finding ways to simplify the process, not expanding it by including additional categories. See our next response for further details.

- *Alternatively, should investments in nationwide funds be attributed to particular states or assessment areas? If so, how can that be done in a meaningful manner, particularly if there is no earmarking by the fund?*

Yes. Banks should have the ability to assign investments in nationwide funds to particular assessment areas based on the statewide or regional areas described in the fund's prospectus

which include those assessment areas. When more than one assessment area is included in the same statewide or regional area identified in the prospectus, the investment should be allocated by any reasonable method determined by the bank, such as the amount of deposits or number of branches in each assessment area. Without assurance of full allocation of the investment, banks will continue to be wary that full consideration is being given to nationwide investments and will decline to invest where there is uncertainty.

- *If nationwide fund investments are attributed to particular states or assessment areas, how can the Agencies avoid double counting the same funds in the same assessment areas in different institutions' evaluations?*

In practice, this issue is irrelevant since many specific property locations are not yet identified at the time of investment. The attempt to artificially parse the investments between banks has created more complexity than necessary, resulting in reluctance to invest in nationwide funds. Each bank should have the flexibility to apply the full amount of the investment to its assessment area(s) included in the same statewide or regional area in a manner that is reasonable and consistent with the intent of the fund's prospectus. If there are concerns about double-counting within specific geographies, the significant opportunity to expand investments to underserved or underbanked markets through nationwide funds will never be realized. In order for these changes to be effective, the Agencies need to provide certainty that banks will receive full consideration for every dollar invested in such funds.

III. Community Services Targeted to Low- or Moderate-Income Individuals

§ __.12(g)(2)-1: *Community development includes community services targeted to low- or moderate-income individuals. What are examples of ways that an institution could determine that community services are offered to low- or moderate-income individuals?*

A1: Examples of ways in which an institution could determine that community services are targeted to low- or moderate-income persons include:

- The community service is targeted to the clients of a nonprofit organization that has a defined mission of serving low- and moderate-income persons, or, because of government grants, for example, is limited to offering services only to low- or moderate-income persons.
- The community service is offered by a nonprofit organization that is located in and serves a low- or moderate-income geography.
- The community service is conducted in a low- or moderate-income area and targeted to the residents of the area.
- The community service is a clearly defined program that benefits primarily low- or moderate-income persons, even if it is provided by an entity that offers other programs that serve individuals of all income levels.

- **The community service is offered at a workplace to workers who are low- and moderate-income, based on readily available data for the average wage for workers in that particular occupation or industry (see, e.g., <http://www.bls.gov/bls/blswage.htm> (Bureau of Labor Statistics)).**
- **The community service is provided to students or their families from a school at which the majority of students qualify for free or reduced-price meals under the U.S. Department of Agriculture's National School Lunch Program.**
- **The community service is targeted to individuals who receive or are eligible to receive Medicaid.**

We support the Agencies' proposal to return to the effective approach used for many years whereby free and reduced-price meals and Medicaid were accepted as proxies for identifying LMI individuals and families. We suggest that these proxies not be limited to CD services, but also be acceptable in qualifying CD loans and investments. Also, language relating to a simple majority should be incorporated in the proposed Medicaid bullet as an option in addition to "targeted to."

- *Will the use of eligibility for free and reduced-price meals and Medicaid effectively identify individuals who are low- or moderate-income?*

Yes. These proxies almost always effectively identify LMI families and individuals. Regarding the free and reduced-price meals proxy, the few areas where the formulaic approach does not work are the very poorest MSAs. The current practice has had a negative unintended consequence of placing those most needy areas at a disadvantage by creating disincentives for banks to engage in CD services in those communities.

- *Will the use of these proxies reduce the burden on financial institutions and community organizations to obtain actual income and, thus, promote the provision of community development services?*

Yes. The information for both the free and reduced-price lunch program and Medicaid is standard, independent and readily available. The ease of use of these proxies reduces burden and allows bank resources to be focused on the actual provision of CD activities.

- *Are there other commonly used proxies for low- or moderate-income that should be specifically included in the Q&A?*

According to the U.S. Department of Education, "the Federal Pell Grant Program provides need-based grants to low-income undergraduate and certain post baccalaureate students to promote access to postsecondary education." The Agencies should review specific income guidelines or the history of recipient incomes to determine whether participation in this program may be a reliable proxy for low- or moderate-income. Also, although not a proxy, we would suggest that activities related to the Earned Income Tax Credit (EITC) be added to the list of examples of community services in § __.12(g)(2)-1. The Internal Revenue Service defines the EITC as "a refundable federal income tax credit for low to moderate income

working individuals and families.” This addition would provide clarity for both banks and examiners and eliminate the need to take any additional steps to qualify such activities.

IV. Service on the Board of Directors of an Organization Engaged in Community Development Activities

§ __.12(i)-3: What are examples of community development services?

A3. Examples of community development services include, but are not limited to, the following:

- **Providing financial services to low- and moderate-income individuals through branches and other facilities located in low- and moderate-income areas, unless the provision of such services has been considered in the evaluation of an institution's retail banking services under 12 CFR __.24(d);**
- **Increasing access to financial services by opening or maintaining branches or other facilities that help to revitalize or stabilize a low- or moderate-income geography, a designated disaster area, or a distressed or underserved nonmetropolitan middle-income geography, unless the opening or maintaining of such branches or other facilities has been considered in the evaluation of the institution's retail banking services under 12 CFR __.24(d);**
- **Providing technical assistance on financial matters to nonprofit, tribal, or government organizations serving low- and moderate-income housing or economic revitalization and development needs;**
- **Providing technical assistance on financial matters to small or community development organizations, including organizations and individuals who apply for loans or grants under the Federal Home Loan Banks' Affordable Housing Program;**
- **Lending employees to provide financial services for organizations facilitating affordable housing construction and rehabilitation or development of affordable housing;**
- **Providing credit counseling, home-buyer and home-maintenance counseling, financial planning, or other financial services education to promote community development and affordable housing, including credit counseling to assist low- or moderate-income borrowers in avoiding foreclosure on their homes;**
- **Establishing school savings programs or developing or teaching financial education or literacy curricula for low- or moderate-income individuals;**
- **Providing electronic benefits transfer and point of sale terminal systems to improve access to financial services, such as by decreasing costs, for low- or moderate-income individuals;**
- **Providing international remittance services that increase access to financial services by low- and moderate-income persons (for example, by offering reasonably priced international remittance services in connection with a low-cost account);**
- **Providing other financial services with the primary purpose of community development, such as low-cost savings or checking accounts, including “Electronic Transfer Accounts” provided pursuant to the Debt Collection Improvement Act of**

1996, individual development accounts (IDAs), or free or low-cost government, payroll, or other check cashing services, that increase access to financial services for low- or moderate-income individuals; and

- **Providing foreclosure prevention programs to low- or moderate-income homeowners who are facing foreclosure on their primary residence with the objective of providing affordable, sustainable, long-term loan modifications and restructurings.**

Examples of technical assistance activities that might be provided to community development organizations include:

- **Serving on the board of directors;**
- **Serving on a loan review committee;**
- **Developing loan application and underwriting standards;**
- **Developing loan-processing systems;**
- **Developing secondary market vehicles or programs;**
- **Assisting in marketing financial services, including development of advertising and promotions, publications, workshops and conferences;**
- **Furnishing financial services training for staff and management;**
- **Contributing accounting/bookkeeping services; and**
- **Assisting in fund raising, including soliciting or arranging investments.**

We support the Agencies' proposal to clarify that serving on the board of directors of any community development organization qualifies as an eligible CD activity. This clarification properly recognizes the consequential fiduciary role of a board member. Serving as a member of the board provides great community value and supports the ongoing success of the organization.

The Agencies request comment on whether there are other activities that should also be included in this Q&A as explicit examples of community development services.

It is generally difficult, if not impossible, to document the revenue sizes of small businesses to which technical assistance is being provided. For example, when a bank sponsors or participates in seminars for small business owners (generally covering topics such as developing business plans, managing cash flow, and other financial management topics), the participants would need to indicate the revenues of their business or the number of employees in order for the bank to make a documented determination. This is at the very least awkward in such a setting and, for many participants, information they may not want to disclose in such a venue. In reality, nearly all such assistance, whether directly provided by the institution or through partnerships with organizations such as SCORE or small business technical assistance centers, is provided to small business ventures, most of which are actually micro-businesses. The guidance needs to be clear that small business technical assistance is presumed to be qualified unless there is evidence that the services are actually being offered or provided to larger commercial enterprises. Such revisions will encourage more small business technical assistance and reduce qualification burdens.

Proposed New Questions and Answers

I. Qualified Investments

§ __.12(t)-9: How do examiners evaluate loans or investments to organizations that, in turn, invest in instruments that do not have a community development purpose, and use only the income, or a portion of the income, from those investments to support their community development purpose?

A9. Examiners will give quantitative consideration for the dollar amount of funds that benefit an organization or activity that has a primary purpose of community development. If an institution invests in (or lends to) an organization that, in turn, invests those funds in instruments that do not have as their primary purpose community development, such as Treasury securities, 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.

- *Is the proposed new Q&A sufficiently clear?*

Yes. The proposed revision is clear and concise.

II. Community Development Lending in the Lending Test Applicable to Large Institutions

§ __.22(b)(4)-2: How do examiners consider community development loans in the evaluation of an institution's record of lending under the lending test applicable to large institutions?

A2. An institution's record of making community development loans may have a positive, neutral, or negative impact on the lending test rating. Community development lending is one of five performance criteria in the lending test criteria and, as such, it is considered at every examination. As with all lending test criteria, examiners evaluate an institution's record of making community development loans in the context of an institution's business model, the needs of its community, and the availability of community development opportunities in its assessment area(s) or the broader statewide or regional area(s) that includes the assessment area(s). For example, in some cases community development lending could have either a neutral or negative impact when the volume and number of community development loans are not adequate, depending on the performance context, while in other cases, it would have a positive impact when the institution is a leader in community development lending. Additionally, strong performance in retail lending may compensate for weak performance in community development lending, and conversely, strong community development lending may compensate for weak retail lending performance.

The proposal appears to make CD lending a requirement. It notes that performance context would be considered, but because the outcome of such consideration is unpredictable, banks would have to assume that it is required in all assessment areas.

Traditionally, the OCC has rated CD lending (as one of the five factors in the Lending Test) as neutral, positive or significantly positive. The new proposal indicates that CD lending could result in negative impact to the Lending Test if the institution's level of CD lending is insufficient. We strongly believe that the OCC approach should not only be retained, but enhanced to provide greater weight to strong CD lending performance. This would be a more effective way to increase the value and overall volume and effectiveness of CD lending than penalizing institutions for inadequate performance.

A new mandate requiring banks to engage in CD lending would run counter to the flexibility the CRA has traditionally embodied. Rightfully, lending activities like mortgage and small business are not required, nor are there volume expectations for these types of lending. There is nothing in the regulation, explicit or implicit, suggesting that CD lending needs to have equal or some other treatment perceived to be similar to the other performance criteria in the Lending Test (i.e., lending activity, geographic distribution, borrower characteristics, innovative or flexible practices).

Requiring CD lending would also have a strong likelihood of leading to unsustainable lending practices. OCC-regulated banks accounted for 44% of all CD lending dollars reported in 2011, the most recent year for which the data is available. In fact, more than one out of every four dollars of CD loans was attributable to eight of the largest banks in 2011, and all those institutions are regulated by the OCC. By requiring higher levels of CD lending and lending in all assessment areas, the consequences will lead to the creation of new "hot spots" where due to CRA, competition reaches levels where unsustainably low pricing and high risk lending is occurring. It would further exacerbate this problem in current hot spot areas already impacted by CRA-caused overheated markets.

In 2011, the average CD loan originated was \$2.6 million. The average CD loan for the top eight banks, all OCC-regulated, was much higher at \$4.6 million. As one would expect, larger banks generally have more capacity to originate these loans safely and soundly due to the cost of maintaining the needed infrastructure to effectively process and manage them. Many of these complex loans require very specific expertise often due to the fact that the debt is leveraged by public financing, e.g. low income housing tax credits, new markets tax credits, stimulus programs, state and local initiatives, etc. At a time when the levels of such public funding are uncertain and even diminishing, this proposal is likely to have the adverse impact of more competition for fewer opportunities. While more pronounced where public financing is a component (due to limited funding), the same unhealthy levels of competition are likely to occur with CD lending beyond publicly-leveraged loans. We believe this is not a sustainable path and truly not the intent of the CRA.

In addition, the proposal does not address how much CD lending would be enough to prevent having a negative impact on the Lending Test. For small business and mortgage lending, the

numbers of loans are significant enough that market and peer comparisons can be useful in many markets. For CD lending, on the other hand, while the dollar amounts can be significant, the numbers of deals are much smaller. And because individual CD loan opportunities and amounts vary widely, so do the totals from one year to another in any particular market. This level of variance would likely ensure even greater uncertainty as to the method of appropriately and objectively rating performance in this particular category. (A key factor in the evaluation of CD lending is the institution's dollar volume. In contrast, mortgage and small business lending are evaluated primarily on their distribution, for which there are well-established demographic and peer benchmarks.)

While we agree that CD lending is not always given the appropriate level of consideration commensurate with its community impact and the complexity and bank resources required, we believe that finding better ways to recognize the significant contribution of CD lending in the evaluation process is the real issue that needs to be resolved. And if the objective of the Agencies is consistency, we strongly recommend, from a safety and soundness perspective alone, movement in the more prudent direction of the current OCC methodology.

- ***Does the proposed Q&A recognize the appropriate value of community development lending, while allowing flexibility based on performance context consideration?***

No. The proposed Q&A does not address the key issue raised by commenters, which is current CD lending activities of banks being undervalued. We believe that banks will engage in sustainable CD lending if it is given more positive weight in the examination. This approach is superior to making CD lending a requirement as we have explained above. In addition, as already noted, the degree of flexibility based on performance context is unclear.

- ***Will this proposed Q&A help to promote additional community development lending?***

There is nothing in the proposal that increases the opportunity for safe and sound CD lending. To promote safe and sound CD lending, the Agencies should instead consider ways to ensure such activities are given appropriate and sufficient positive consideration in the existing framework of the regulation, the primary concern previously raised by commenters. If participation in CD lending is retained as optional, and there is more flexibility for CD activities including those located in greater statewide or regional areas that include assessment areas, banks would be more likely to find prudent and measured ways to match those benefits with viable lending opportunities.

- ***Does this proposed Q&A appropriately clarify the consideration given to community development lending as one of the five performance criteria under the lending test?***

No. The proposed language does not clearly indicate whether CD lending is required because of the reference to Performance Context. Since history shows that treatment of performance context is subjective and inconsistently applied, banks would have to assume that CD lending is a requirement if the proposed language is adopted. Mandating this activity would be an expansion of the CRA that does not align with the intent of the law.

There is no such requirement that banks engage in mortgage or small business lending, and for OCC-regulated banks there has never been a mandate requiring CD lending. The top eight banks (all OCC-regulated) by CD loans reported in 2011 accounted for just over 25% of all CD loans reported for that year. Further, all OCC-regulated banks accounted for more CD lending (about 44% of the total) than either Fed- or FDIC-regulated institutions. It is clear the OCC's examination process of providing either neutral or positive consideration for CD lending has not hampered the amount of CD lending by banks within their jurisdiction. Given the proposal's significant expansion for the largest part of the industry, it could very well lead to more competition for the same opportunities or cause more marginal loans to be made with higher levels of credit risk and unsustainable pricing. The ultimate result of greater risk and unprofitable lending runs counter with the safety and soundness language in the CRA statute. We would recommend that if the true objective is consistency between the agencies, consideration be given to adopting the more prudent OCC methodology and then addressing the heart of the concerns raised by previous commenters by proposing ways to ensure that CD lending activity is given appropriate positive consideration in the evaluation process when warranted.

- *Does this proposed Q&A raise any issues that the Agencies will need to address with revised ratings guidance? If so, what are they and how should they be addressed?*

The largest issue to be resolved within the proposal is whether CD lending activity would be required, and if so, the activity level needed to prevent negative consequences or attain a positive result in the evaluation. Quantitative measurements of performance at an assessment area level are challenging due to: a) relatively small numbers of loans in any given year, b) varying opportunities from year to year, and c) wide ranges in individual loan amounts. As for the qualitative components including responsiveness, complexity and leadership, the complete impact of much of this type of lending is very difficult to fully convey in the evaluation process. To compensate, banks often provide the opportunity for examiners to see the positive community impacts firsthand by providing on-site tours. However, if CD lending becomes required in every assessment area, this firsthand approach would be impractical for the largest national and regional banks that originate much of this lending due to their large numbers of assessment areas. Given these complexities, how would the Agencies make certain that examiners possess the necessary expertise and knowledge of each local market to ensure sound rating results? The level of uncertainty associated with this approach could lead to banks overcompensating by irrationally increasing their CD lending, an outcome that would not lead to sustainable CD lending in underserved neighborhoods or to underserved populations.

In summary, our key concerns with the proposed Q&A § __.22(b)(4)-2 are:

- Considering that the OCC has never before mandated any type of lending, requiring CD lending would increase competition to unhealthy levels and be a significant expansion of CRA for OCC-regulated institutions. Further, it would be inconsistent to require CD lending but not mortgage or small business lending. Requiring one type of lending but not another would also undermine the intent of CRA.

- o Penalizing institutions is not an effective way to encourage more safe and sound CD lending. Many institutions do not have the necessary expertise or infrastructure to make complex CD loans, price them appropriately, and manage the associated risk, thereby jeopardizing market stability and sustainability. Rather, encouragement should only be in the form of heavier weighting for positive performance.

General Comments

The Agencies invite comments on any aspect of this proposal. The Agencies particularly would like comments on those issues specifically noted in this supplementary information section.

Steps should be taken to minimize the burden of the CRA Public File, considering that much of the information is readily available elsewhere. An example worth considering is the possibility of not having to list products and services if that information is available on the bank's website. A similar example applies to the HMDA and CRA small business disclosure requirements, as this data is available at the FFIEC's website.

We also suggest that banks receive consideration for *pro bono* services (e.g. legal, personnel or IT services) provided to CD organizations. These types of volunteer services are highly valued by CD organizations and help them build capacity to more effectively serve their existing clients or expand their clientele. However, this is similar to the Public File in that it would likely require a regulatory change due to the current stipulation that activities must be related to the provision of "financial" services.

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Again, thank you for your efforts to strengthen this very important regulation and the opportunity to comment on the proposal.

Sincerely,



Dorothy Broadman
Senior Vice President & CRA Officer
Community Development Banking