AMERICAN BANKER®
THE FINANCIAL SERVICES DAILY

Monday, November 03, 2014

BANK THINK

How to Move the CRA into the 21st Century

By Warren W. Traiger

There's a disconnect in the banking agencies' approach to reforming the Community Reinvestment Act.

On the one hand, the Federal Reserve, Office of the Comptroller of the Currency and Federal Deposit Insurance Corp. propose moving the CRA into the 21st century by deemphasizing branches as a means of serving lower-income neighborhoods and individuals. In their recent proposal to amend CRA regulatory guidance, the agencies note that there "are effective alternatives [to branches] in providing needed services to low- and moderate- income geographies and individuals." They specifically cite "technological advances in the retail banking industry, such as Internet or online banking, mobile banking, remote deposit capture and 24-hour Internet banking kiosks."

On the other hand, the starting point for determining the communities in which a bank has CRA obligations remains rooted in 1977, the year the law was enacted. A bank's assessment area is delineated based on where a bank has a physical presence. That a bank may engage in nationwide lending or deposit-gathering through the technological advances listed by the regulators is irrelevant to defining its assessment area.

As a result, banks only have formal CRA responsibilities in the areas surrounding their headquarters or deposit-taking facilities. Never mind that a bank may have a single office in an out-of-the-way location. Never mind that the office may not be open to the public. And never mind that a bank may only do a small fraction of its business near the office, while making the vast majority of its loans and receiving deposits in areas hundreds of miles away.

The agencies recognize and understand this issue. Indeed, geographic coverage was the lead issue when they held a series of public hearings "on modernizing the regulations that implement the CRA" back in 2010. The agencies received testimony on questions about whether geographic scope should be defined differently for institutions with limited or no physical deposit-taking facilities and for small, local banks as compared to nationwide banks.

Warren W. Traiger is Counsel in the New York office of Buckley Sandler LLP.

But so far there's been radio silence on the answers to these questions. Instead, the agencies have engaged in regulatory contortions to apply the current assessment area rules to non-traditional institutions.

For example, public performance evaluations of nationwide lenders without meaningful branch networks rationalize the inclusion of out-of-assessment area performance with statements like, "As [the bank] is a nationwide lender, not restricted to any geographic locale and without any physical branches, additional consideration was given to certain activities conducted in a wider regional and nationwide area." Another evaluation explained that "a broader analysis of [the bank's] national lending was conducted to demonstrate that the bank's overall performance was consistent with its lending in the designated assessment area."

These contortions may be necessary to conduct meaningful CRA evaluations of nationwide lenders that have little or no brick and mortar presence, but they are no substitute for amending CRA regulations and guidance. Jerry-rigged examinations lack the legal foundation that provides banks with an understanding of what compliance efforts are necessary to achieve acceptable CRA performance.

This problem cannot be resolved by adopting a CRA strategic plan, an option that regulators sometimes suggest to nontraditional banks as a means of providing compliance certainty. A strategic plan, developed by a bank in conjunction with its community and regulator, that includes lending, investment and service goals for communities outside the assessment area is no less problematic than examinations that gloss over the letter of the law.

There is a relatively easy solution to this problem—one that is consistent with the existing CRA framework that recognizes that not all banks should be subject to the same CRA rules. Regulators should simply carve out a category of virtual banks that have tailored CRA responsibilities and examination standards.

Right now, banks that do not deal with the retail public and banks with a narrow product line already have their own designation and exam procedures. Once designated by their regulator as wholesale or limited-purpose, these banks may receive CRA consideration for activities conducted anywhere in a multi-state region that includes their assessment area. Then, provided the multi-state activity is adequate, the banks get full credit for CRA-related activities conducted nationwide.

This approach can be readily adapted to virtual banks. Once designated, a virtual bank that provided adequate CRA lending, investment and service to the region in which its office was located would also receive consideration for CRA activities conducted elsewhere—that is, the additional places where the bank conducts the bulk of its deposit and/or lending business.

Developing distinct examination rules for virtual banks make sense for the same reason it makes sense to have different examination standards for other non-traditional institutions: the CRA works better when its rules are not one-size-fits-all. This philosophy was the basis for providing different treatment for wholesale and limited-purpose institutions when the regulations were last substantially revised in the mid-1990s. Applying this approach to virtual banks today will help advance an objective shared by banks, regulators and community advocates—moving CRA compliance into the present day. ▪