# SAN DIEGO CITY-COUNTY REINVESTMENT TASK FORCE

**April 8, 2020**

## Comment regarding Community Reinvestment Act (CRA) Regulations
## Docket ID OCC-2018-0008

On behalf of the San Diego City-County Reinvestment Task Force, we are writing to register our opposition to changes to the Community Reinvestment Act proposed in the draft rule. The Community Reinvestment Act is the most American of laws, encouraging banks to serve all people and neighborhoods, regardless of wealth. Any changes to CRA must honor and expand on the original intent, purpose, and legislative mandate of the law – building low and moderate-income people's credit, financial strength and housing stability – not weaken and undermine it, as the proposed rule does. The work of CRA has not been completed. There is still much to do.

The San Diego City-County Reinvestment Task Force is a 43-year-old, joint City and County Commission tasked with monitoring banks' CRA activity in our region. Our stakeholders and 15 appointed board members, representing public, private and nonprofit organizations active in affordable housing, small business, home ownership and community development, work to increase bank reinvestment across San Diego County, the fifth-largest county in the United States with 3.3 million residents. Our members include representatives of local government, the nation's largest banks, affordable housing providers like Wakeland Housing and MAAC Project, and the local offices of national community development nonprofits like Accion and LISC.

The RTF's work includes programs that increase opportunity in low and moderate-income (LMI) communities, investigating emerging affordable housing funding sources, and promoting innovative ideas for improving the economic lives of the San Diego region's low and moderate-income residents. We produce yearly assessment that tracks, analyzes and charts more than $3.4 billion in annual countywide CRA activity by our national bank partners. We are committed to the goals of CRA and deeply invested in seeing CRA's tools used to improve the lives of San Diego County's low and moderate-income residents through family asset building, affordable housing and small business ownership.

## Updates Must Prioritize CRA's Original Purpose.

We are deeply concerned that the proposed changes to CRA will undermine its original intent by changing how banks' CRA activity is evaluated and, more alarmingly, by expanding this historic law to include activities that stray far from CRA's founding purpose. That purpose, which must remain central, was to extend lending to LMI persons and neighborhoods, even if those loans and investments were less profitable than serving wealthier customers. This was our nation's direct and proper response to the redlining of the past. Since 1977, trillions of dollars have flowed into LMI communities because of CRA. In San Diego County alone, it resulted in more than $25 billion in loans, investments, and grants from 2013-2018 that directly improved the lives of LMI families, an enormous impact.

We also believe it is the wrong time, amid a national health and economic crisis, to pursue changes to one of the nation's most crucial banking laws. The country and its leadership are marshaling all available resources to combat the novel coronavirus pandemic, and that is where their attention should remain, not on enacting

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unrelated significant regulatory change. Our nation is still far from knowing how devastating the economic impacts of Covid-19 will be. Any update to CRA must take into consideration the economic environment that emerges from this unprecedented time.

If and when the three Federal financial supervisory agencies move forward with the rule-making process, we urge them to strengthen CRA in the following ways:

## 1. Preserve CRA's Historical Focus on Serving Low and Moderate-Income Americans.

The sole criterion for giving CRA credit to a business activity should be its direct, significant, and exclusive benefit to LMI people, in keeping with the original intent and purpose of CRA.

Extending CRA credit to activities that benefit middle-income people or only partially benefit LMI people is CRA mission creep away from the core tenants of the law. The positive impact on LMI people – not on middle-income populations, all incomes if a project has a community purpose, or projects that partially, not principally, benefit LMI people – must be the central requirement for CRA qualification.

By continuing to focus CRA activity only on persons making up to 80% of area median income (AMI) – the CRA definition of LMI – the law will create a beneficial continuum of support. This continuum will help both the very neediest (those making up to 60% of AMI), as well as those working class families (60-80% of AMI) who are stuck on the first rung of the asset-building ladder and are beginning to build their financial foundation. Together, these groups making up to 80% of AMI should be the sole beneficiaries of CRA activity.

## 2. Do Not Expand CRA's Definition of "Allowable Activities."

We are strongly opposed to the dilution of current CRA activities by expanding the definition of what is allowable under CRA. The new rule suggests extending CRA credit to such activities as funding for "essential" infrastructure and facilities like bridges, schools, police and fire stations, parks, libraries, telecommunications infrastructure, roads, tunnels, mass transit, sewage treatment, water supply and distribution. This broad list will divert funding from traditional community development activities like affordable housing developments to huge, expensive public works projects that do nothing to relieve rent burdens or build family self-sufficiency, which is the original intent of CRA.

The proposed expansion adds new categories of eligible beneficiaries. It appears to facilitate self-dealing by offering banks CRA credit for providing homeownership seminars to their customers, regardless of whether the customers are LMI or not. It further relaxes CRA's historical focus on low and moderate-income persons by adding all family farms as a general category of eligibility. (In 2015, the median wealth for family farm operator households was $827,300, according to CNN.)

Most of all, extending CRA credit to activities that increase gentrification, such as Opportunity Zone financing for luxury housing, is counterproductive to the aims of CRA. The proposed rule asserts that the newly-added activities "are consistent with the purpose of the CRA." We would strenuously disagree and warn that such activities will adversely affect LMI populations.

Put together, the expanded list of activities reduces financial institutions' incentives to invest in traditional CRA-eligible projects. Banks will look elsewhere for their business and turn down traditional CRA projects because they have other easier and more profitable options. However, that's the whole point of CRA: to

provide an extra incentive to undertake lending and investment that is valuable to society but generates lower profits. Banks do not need CRA's incentive to pursue the kinds of projects and populations that have been proposed to be added to the law.

If the regulators nonetheless proceed with an expanded list of eligible activity, we urge them to trade currently eligible low-impact activities like loan purchases in exchange for adding new CRA activities. Furthermore, any new activities, if ultimately added should be given significantly reduced weight compared to traditional CRA activities, and then reduced further by the pro rata multiplier proposed in the rule. For example, if the agencies want to recognize bank activity that has a distant community development purpose, they should assign the new activities 20% of the value given to original, higher-impact activities, so they do not dilute the incentive to meet still-critical credit needs for subsidized affordable housing, LMI homeownership, and very small business loans.

Most important, however, we question the premise that new CRA-eligible activities are needed so that more CRA activity can occur. If more activity occurs but it lacks strong and positive community impact for LMI people – or worse, contributes to gentrification, higher rents, and displacement – the increase in activity is meaningless.

It is true that stakeholders, including us, spoke of the need for more lending and investment in areas served by CRA. However not just any lending and investment, but those activities that specifically reduce the cost of housing for LMI families or push asset-building capital into the hands of LMI Americans who continue to have their needs neglected by financial institutions.

Instead, as written, our concern is that the proposed rule would let banks earn all of their CRA activity in the new expanded activity areas and populations. Let us save that for when all of the credit needs of the current activity areas and populations have been met, as we are currently far from that goal. Expanding eligible activities neglects the unmet credit needs that existed before and continue to persist.

## 3. Do Not Expand the Definition of "Affordable Housing."

We believe the proposal to relax the definition of community development loans for an affordable housing purpose – traditionally income-restricted, subsidized affordable housing – is deeply misguided. Funding activities like nursing homes, middle-income housing in high-cost areas, and naturally-affordable housing (defined as rents that are currently affordable, but not restricted, to LMI families) in any census tract will siphon capital away from critical housing projects that provide permanently affordable apartments to LMI families.

Subsidized affordable housing projects are already incredibly hard to finance, and this change will reduce bank interest in pursuing these loans, raise financing costs, or worse, prevent these projects from acquiring the financing they need to come to fruition at all.

Also, adding new CRA-eligible activities will reduce demand for Low Income Tax Credits and further decrease their value – already dampened by the change in incentives created by federal tax reform. Together these impacts increase the subsidy required from local government to make affordable housing deals pencil, which will have a crushing impact on high-cost regions like San Diego. Since governments have a limited pot of money from which to help fund housing projects, increasing the size of the required subsidy means that fewer affordable housing units will be built.

Other proposals in the new rule will further raise the cost of building subsidized affordable housing. Plans to combine the Community Development Lending and the Investment categories into one, instead of evaluating the volume of activity in each category, will increase the incentive to focus on whichever of the two financing tools is easier – loans or investments – to the detriment of the other, equally-needed form of affordable housing finance. This too will raise project costs and decrease construction.

The need for subsidized housing in LMI communities is tremendous. In San Diego County, the Reinvestment Task Force's six member banks financed a record $496 million in loans for these kinds of projects in 2018. Yet in California's overheated housing markets, even nearly $500 million a year still isn't enough to build affordable housing fast enough to dent demand. San Diego and other regions need CRA to maintain and increase the number and value of loans for rent-restricted affordable housing.

## 4. Don't Expand Who is Eligible for CRA-Qualified Affordable Housing.

The proposed rule creates new populations who can benefit from CRA activity and changes the way subsidized affordable housing is evaluated under CRA. One proposal, financing middle-income housing for middle-income individuals in high cost-areas, was never the intent of CRA and has nothing to do with building financial strength and self-sufficiency for LMI people. Adding new categories of beneficiaries would re-write the fundamental purpose of CRA. There is no doubt that middle-income groups are discouraged by high housing prices, but relieving high housing prices for them is not the purpose of CRA and will shift capital away from much needier populations.

## 5. Offer Double Credit for Originating Loans to LMI Homebuyers.

The most essential, most-needed CRA mortgages are those for the LMI homebuyers' original home purchase. Home purchase mortgages are more challenging to underwrite than refinancing or home improvement loans and should get twice or more CRA credit in order to incentivize banks to increase their originations of these loans.

In the San Diego MSA, a region with 3.3 million residents, the Reinvestment Task Force found that in 2018, the six largest national banks originated only 192 home purchase loans to LMI borrowers or four percent of all their home purchase loans. Non-bank lenders, with their less-attractive terms and higher interest rates, were our region's largest originators of LMI loans for a home purchase. We need the banks to be more active in this space, and continued CRA incentives and monitoring will help this to happen.

## 6. Cap Mortgages for Non-LMI Borrowers in LMI Census Tracts.

We support the proposed rule's recommendation to remove CRA eligibility from mortgages provided to non-LMI homebuyers in LMI census tracts. These kinds of loans personify gentrification and lead to displacement. However, discouragingly, the anti-gentrification benefits of this action are undermined by giving CRA credit for all Opportunity Zone lending and investments, regardless of positive – or more often, negative – impact on LMI people.

Furthermore, the good done by removing CRA credit for non-LMI homebuyer loans is more than offset by proposals to extend CRA eligibility to middle-income populations and naturally affordable – but not permanently affordable and income-restricted – housing.

If regulators want to help middle-income residents, regulators could cap eligibility for non-LMI home borrowers in LMI census tracts at 120% of AMI, instead of eliminating CRA eligibility for these borrowers entirely. In addition, loans to middle-income homebuyers who fall within 80-120% of AMI could receive partial CRA credit, instead of the full credit provided to loans to LMI persons.

We support this limited exception for middle-income housing because it is already part of CRA and, more important, we believe it will reward banks for helping middle-class African Americans and Latinos, who have much lower home ownership rates than Whites, to achieve homeownership and narrow the racial wealth gap.

## 7. Reduce or Eliminate CRA Credit for Other Low-Impact Activities.

Purchases of mortgage-backed securities and loans originated by another financial institution are low-impact CRA activities and should be disallowed or given diminished credit.

Similarly, low-impact activities like financing non-income restricted apartment buildings in LMI census tracts should be disallowed or given diminished credit, particularly in active, high-cost real estate markets.

## 8. Do Not Rely on an Over-Simplified Single Metric/Evaluation Ratio.

The new Single or One Ratio metric (single CRA evaluation measure) is opposed by us and the vast majority of commenters because it will incentivize expensive, higher-profit activities and larger, easier transactions at the expense of lending activities that have the greatest impact on improving the housing security and financial health of LMI people: loans for much-needed affordable housing, smaller-dollar home mortgages and small business lending – three crucial areas of family stabilization and wealth-building.

The single metric doubles down on the very thing – larger loans – that profit-seeking already incentivizes. Banks do not need an additional reward to pursue large, high-profit lending. San Diego County and communities across the country need CRA in order to level the playing field and incentivize higher-impact, lower-profit lending and community development activities.

If a single evaluation measure is used to determine a bank's CRA rating despite widespread opposition, the level of activity required to achieve an Outstanding or Satisfactory rating should be set high, especially if new, expanded categories of activity are allowed. Also, high minimum activity levels for achieving each rating should be set not only for the sum total of investment but for each major activity category.

## 9. Measure and Evaluate Each CRA Sub-Activity Area Separately.

The distribution of a bank's CRA activity is equally important as the sum total of its activity. We believe banks must be evaluated in each CRA activity area, with a high minimum threshold of activity, by the percentage of deposits, in each area.

At the San Diego City-County Reinvestment Task Force, we love metrics. We use them ourselves and calculate a local version of the proposed CRA evaluation measure by both dollar value and as a percentage of each bank's local deposits. However, we do the same for each of the main categories of CRA activity, calculating the number, value, and percentage of deposits assigned to home mortgages (by each loan type), small business loans (split into larger loans/enterprises and the smallest loans and enterprises), small farm

loans, tax credit affordable housing lending and investment, other community development lending, and CRA-qualified philanthropic giving.

The regulatory agencies must do the same, measuring and assessing CRA activity in each category, not just the sum total of all activity. Furthermore, activity levels should be measured by both quantity and value, as the Reinvestment Task Force does, to guard against doing fewer, larger loans and investments.

## 10. Build in Protections Against Unintended Consequences.

The proposed rule is rife with opportunities for unintended consequences. Regulators must guard against these potential negative impacts by anticipating them and adjusting the assessment algorithms. For example, will community development lending get reallocated to lower-impact activities if the definition of CRA-qualified activity is expanded, leaving traditional CRA lending needs unmet?

If a bank has an average annual total of community development lending for the past three years under current CRA rules, that prior average should be adjusted upward to reflect the expansion of allowable CRA activity. Then that new, adjusted total should be the dollar amount benchmark for receiving the same rating that the bank achieved in prior years to ensure that the same amount of traditional community development activity is performed before and after the rule change.

More important, what guardrails will the regulators put in place to prevent a financial institution from doing half the work it did before if the new rule lets that institution receive double credit for some of its activities? Will banks reduce their subsidized affordable housing development lending by half when those projects qualify for twice the credit than they did before? Threshold minimums for achieving an Outstanding rating must be calculated by taking prior year activity and adjusting it upward by the same multiplier.

## 11. Retain a Focus on Bank Branches in LMI Neighborhoods.

The presence of bank branches in LMI communities is extremely important. In San Diego, LMI residents have a greater reliance on in-person banking at their branch. Furthermore, they are more reliant than other customers on public transit, which limits their ability to access a non-neighborhood bank branch.

Yet the proposed framework devalues bank branches in LMI communities and basic bank accounts for LMI customers. Moving to this approach will significantly diminish the importance of bank branches within the CRA evaluation, which will lead to significant branch loss in LMI communities. This will be followed by a decrease in lending, which is contrary to the goals of CRA.

## 12. Don't Increase the Size of "Small" Businesses and Family Farms. Give Double Credit to the Smallest Small Business Loans.

We are deeply opposed to expanding the definition of small business by raising the already-high revenue threshold from $1 million to $2 million. There is a crisis in truly small business lending and the existing cap of $1 million is already too high, pushing lenders to the largest small business loans.

Instead, the financial regulators should reward and incentivize banks by providing them with double credit for the smallest small business loans. Small business loans of less than $100,000 are the most challenging and

expensive loans to underwrite, and yet are the ones most needed for small business creation and expansion, and the hardest loans to get approval for.

Giving CRA credit for larger loans and to larger "small" businesses doesn't require heavy lifting by banks and doesn't need incentivizing. CRA needs to provide incentives for serving the smallest farms and small businesses: They are deeply underserved. Raising the loan and enterprise size for small business and family farms will incentivize banks to seek their CRA credit from the largest, easiest-to-serve borrowers. That was not the intent of CRA – just the opposite.

## 13. Don't Give Banks High CRA Ratings Based on Half Their Assessment Areas.

We believe that no bank should be given a rating of Outstanding or Satisfactory if their performance in up to half of their assessment areas is below "satisfactory," as proposed in the new rule. By law, CRA requires banks to meet the credit needs of *all* of its communities, including the less (but still) profitable ones. A bank can't cherry pick the best and richest customers or geographic areas.

Yet under the proposed rule, banks only need to achieve a rating of Outstanding or Satisfactory in half or more of their assessment areas to get one of those two highest ratings overall. A rationally-acting bank could then focus all of its CRA efforts on half of the country based on preferred geography, ease of undertaking CRA activity, or the impact on its bottom line of pursuing CRA activities in that region versus another, and completely ignore the CRA needs of up to half of their markets.

This is MSA-level redlining – the very thing CRA was created to combat – and would artificially redirect CRA capital flows away from some regions to a limited number of chosen ones.

## 14. Evaluate All Banks Every Three Or Four Years, Not Five.

Banks with an Outstanding rating should still be evaluated once every three or four years, not the five years that is proposed. We recognize that giving fewer exams does reward and incentivize Outstanding performance. However, that's already what the "Outstanding" rating is supposed to do. It should be its own reward, both in terms of reputation and in CRA enforcement when mergers and branch changes are considered.

We also urge the regulators to ensure that the exam process continues to offer plentiful opportunities for meaningful public input regarding a bank's performance.

## 15. Incorporate the Federal Reserve's Proposals Into the Final Rule.

We support the Federal Reserve proposals, outlined by Governor Lael Brainard, which would more accurately evaluate the CRA performance of financial institutions and continue to prioritize the positive and direct impact of a CRA activity on the lives of LMI people. In particular, we recommend that the final rule:

- Evaluate lending by the number, not only value, of home mortgage and small business loans "in order to avoid inadvertent biases in favor of fewer, higher-dollar value loans," as we do in our own annual San Diego region report;

- Analyze separate metrics for each of a bank's major product lines in its CRA performance, instead of totaling up the dollar value of all its CRA activity in that assessment area; and
- Measure home lending performance by creating a borrower distribution metric that calculates the percentage of a bank's number of loans made to LMI borrowers relative to its overall number of mortgage originations, as we do in our report. (We also evaluate each bank's number of loans for home purchase separate from refinance and home improvement loans.) In addition, we calculate the average loan size for both mortgages and small business loans, giving the highest value to smaller loan balances, which show greater community responsiveness and bank effort than large loan balances.

## 16. Enact a Unified Regulatory Standard.

We support a uniform, consistent set of rules that is shared and implemented by all three regulatory agencies, and not two separate systems for the nation's banks. Parallel regulatory regimes would be inefficient, chaotic and unequitable.

## Strengthen CRA by Retaining Its Primary Focus on Serving LMI People.

More than 40 years after CRA's passage, small businesses, affordable housing developers, and LMI homebuyers in the San Diego region and across the country still struggle to get financing. Yet the regulators' proposed rule would fundamentally change the purpose of CRA, directing its incentives away from increasing lending to LMI people and projects that directly and primarily serve LMI people, especially with respect to providing affordable housing for them. We believe this will result in fewer loans that specifically benefit members of LMI communities.

Instead of mortgages to help low and moderate-income families join the middle class in homeownership, the rule will encourage banks to shift to helping middle-income teachers and public safety officers buy homes in expensive markets. Instead of financing tax credit affordable housing projects, banks will finance market-rate housing, schools, and public works infrastructure. These are all worthy needs, but CRA was never intended for them, and they will divert funding from the needs that CRA was created to address.

The goal of CRA is to ensure that low and moderate-income families like the San Diegans we work with and represent have access to wealth-building tools like home mortgages and small business loans, and that there are market incentives through CRA for banks to finance rent-restricted affordable housing. We must retain a laser-like focus on these goals until there no longer is a need for them.

When the original purpose of the CRA still hasn't been fulfilled, we wonder why the federal financial regulators believe the time is right to move on from these goals. That is what this proposed rule would do, shifting capital flows away from these core needs to more financially-attractive but lower impact lending and investment opportunities.

Instead, raise the bar. We'd like to see the banks incentivized to do even more, not less, providing millions of dollars more each year in home purchase loans for LMI borrowers, small business loans under $100,000, and tax credit investments and multifamily loans that build the thousands of affordable housing units that San Diego County and much of the country need.

Our region is unified in asking the federal financial regulators to retain CRA's priority and focus on the traditional activities that directly benefit LMI families. LMI communities have the greatest financial needs and the highest barriers to opportunity and credit. Only when these needs have been met can other qualifying activities be considered for addition to CRA.

Like the rest of America, San Diego's middle class has been hollowed out by economic, political, and technological changes, pushing families down the income and wealth ladder. CRA is how we can help more San Diegans and other Americans re-build their financial stability and family wealth by starting small businesses, securing affordable housing, and moving up into homeownership. CRA is how we rebuild America's middle class.

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