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"THE COMMUNITY REINVESTMENT ACT:
WHAT ROLES FOR CONSUMERS?"

by

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I am delighted to be here today to talk with you on a topic which continues to attract a lot of attention -- the Community Reinvestment Act.

As you know, last year the CRA was amended for the first time in its thirteen-year history. The Act as amended requires the banking agencies to make CRA Evaluations available to the public, for all CRA examinations conducted after July 1, 1990. It also changes the system the agencies use to rate the CRA performance of financial institutions.

Even with these changes, the CRA's actual legal requirements are relatively few in number and quite straightforward. And, most importantly, the burden of these legal requirements still falls on the bank supervisory agencies.

Let me explain.

The "Requirements" of CRA

First, the CRA requires the banking agencies to encourage financial institutions to help meet the credit needs of their entire community, including those of low- and moderate-income neighborhoods, but to do so in a way consistent with safe and sound practices. That hasn't changed.

Second, the CRA still requires the banking agencies to assess the performance of financial institutions in meeting those credit needs. We do this through examinations, the results of which are now made public.

Finally, the CRA still requires the agencies to consider the CRA performance of financial institutions when reviewing their applications for expansion of depository facilities through branching, mergers, or acquisitions. But, it is important to remember that the Act does not require denial of an application solely because the institution's CRA performance is deficient. The results of these application decisions have always been public.

In discharging their responsibilities, of course, the agencies have implemented regulations which do impose specific requirements on banks, but these are essentially technical and procedural.

For example, each bank must develop and update a CRA Statement, delineate its community, post CRA Notices in the lobbies of depository facilities, and maintain a Public Comment File which may be inspected by the public and the banking agencies. With disclosure, the agencies now require banks to make public their CRA Evaluations within 30 business days of their receipt from the agencies.

In brief, those are the key requirements of the Act and the agencies' regulations. In reviewing them, it is important to remember several things which the Act does <u>not</u> require, even as amended.

First, CRA <u>does not require</u> any one bank to make each and every type of loan that a bank can make or meet all community credit needs by itself. Some banks focus on retail lending to consumers, some specialize in small business lending, while others cater to the wholesale needs of commercial customers. Some banks make mortgage loans, and others do not.

Second, CRA <u>does not require</u> banks to make any specific number or proportion of loans to certain types of individuals, groups, or businesses. It <u>does not require</u> banks to make any proportion of loans in any particular geographic area. Congress consistently has rejected schemes which would mandate credit allocation.

Third, CRA <u>does not require</u> banks to make loans at below-market interest rates, or under terms and conditions inconsistent with safe and sound lending. CRA does not require banks to give money away even for the worthiest of causes, though some banks do. Although some banks have been willing to set aside special, reduced-rate financing for certain community development purposes, they are not required to do this by the CRA or any other law. These kinds of decisions continue to be totally within the discretion of the bank.

CRA As A Process

Well then, what is CRA really about? It is clear that for banks, the essence of CRA is not necessarily contained in what its old and new provisions require or do not require. To focus only on those narrow requirements is to miss the point.

I believe that CRA is a process -- a process that involves rights, responsibilities and, especially, relationships in our economy and our banking system. It is not just legal requirements. The key, however, is the result of that process -- financial products and services which are responsive to community credit needs.

In essence, CRA says that with the rights conferred on them by their charters, financial institutions also have responsibilities to meet the convenience and needs, including the credit needs, of their communities. They have the responsibility to conduct real and serious assessments of the credit needs of their entire community. And they have the responsibility to develop and affirmatively market products and services that help meet those community credit needs, including the legitimate needs of economically disadvantaged persons or areas.

CRA affirms that banks have ongoing responsibilities to maintain relationships with their communities. Although these relationships take many forms, they are in the final analysis business relationships which focus on the need to know and effectively serve a market and its sub-markets.

To know their markets, banks must establish communication with customers and potential customers. Banks must actively seek working relationships with local governments and community, business, and consumer groups in order to identify community credit needs.

Only by developing and nurturing those working relationships within their communities can banks develop responsible programs and loan products to respond to community needs.

Significant Progress

How well is the CRA process working and what are its products? Well, banks have always served their markets and paid attention to community credit needs. Bankers have recognized that the economic, physical and social health of communities affects the health and profitability of banks in those communities.

But I also believe that in recent years a combination of higher expectations and greater effort has resulted in significant additional progress in community reinvestment.

Over the last few years, CRA has encouraged development of programs which probably have stimulated several billion dollars of bank loans for home mortgages, housing construction and rehabilitation, small and minority business development, and revitalization of commercial areas in low- and moderate-income communities throughout the country. Commercial banks and thrifts have developed innovative and successful public-private partnerships which are helping rebuild urban neighborhoods and rural communities. An increasing number of banks have formed community development corporations or invested in equity pools aimed at supporting projects benefitting low- and moderate-income areas. Banks and thrifts also have formed a growing number of lender consortia to pool resources and share risks while working on community credit needs. After what are sometimes adversarial beginnings, banks and community groups have demonstrated over and over again that they <u>can</u> work together to promote the goals of the CRA process.

On the one hand, I believe that banks in recent years have accomplished much more than they take or get credit for. And much of what has been accomplished can be attributed to an increasing awareness of their responsibilities under CRA.

On the other hand, CRA ratings indicate that some banks are still doing less than they should and could do.

For the CRA process to work, the Federal Reserve System and other banking agencies also realize that we have to do our jobs professionally and consistently. And although there may be room for improvement, I think on balance we are.

I am aware that the agencies have been criticized in the past, and sometimes justifiably so. But I believe that this criticism often ignores the truly hard work we have been doing on a day-to-day basis. Let me review some of that with you.

The Regulators' Roles and CRA Disclosure

For example, the Federal Reserve System has Community Affairs Officers and programs in each Federal Reserve District Bank. As part of our CRA "Encouragement" program, they provide information and advice to banks on CRA and community development matters, work with community organizations, and help banks and community groups work together. They also help train our examiners. Through these activities, as well as conferences and publications, our Community Affairs programs have reached thousands of bankers, local government officials, and consumer and community groups and their members. I believe we have made a difference.

The Federal Reserve System also allocates substantial training time each year to our compliance examiners -- just on CRA. That is in addition to the training examiners receive on the myriad of other consumer laws for which they are responsible. This training is important because the Federal Reserve System has conducted separate and focused consumer compliance examinations, which include CRA assessments, for more than ten years.

We are also taking steps to help our safety and soundness examiners understand the essentials of the community development market so they can accurately assess the quality of a bank's CRA loans. As you know, there is growing concern over the health of real estate finance markets nationally and regulators are looking very closely at real estate loans. But we also want examiners to recognize that there is tremendous demand for low- and moderate-income housing and other neighborhood revitalization projects and public-private partnerships are providing affordable financing on a safe and sound basis. In other words, we believe that there need be no conflict between CRA and safety and soundness.

With respect to CRA disclosure, the Federal Reserve, and all of the other agencies, have devoted significant training resources to ensure that examiners understand the new CRA rating system and the disclosure process. We are spending a lot of time reviewing the public CRA Evaluations to ensure that they are comprehensive, clear, and responsive to provisions of the law.

Since July 1, the Federal Reserve System has completed and released to banks for their disclosure over 196 CRA Evaluations. Overall, the process seems to be working well, but, like all new programs, it is open to improvement. Our own Consumer Advisory Council has conducted a preliminary review of some of the early CRA Evaluations and has made suggestions which are now being considered. We believe many of these suggestions will strengthen the process.

The banking agencies do want to be responsive to public concerns about the CRA disclosure process. In fact, one improvement to the process is already being implemented. It will provide the public with easier access to CRA Evaluation reports.

The procedures originally adopted were designed to make each bank's CRA Evaluation report available to those most directly affected by the bank's CRA performance -- that is, the community in which the bank operates. Under those procedures, CRA Evaluations are sent to the banks which, after thirty business days, must release them to the public upon request. The public is told about the existence of the Evaluation and where to obtain it through notices posted in bank lobbies.

The problem with those procedures was that consumers had to either visit bank lobbies or call the banks and supervisory agencies frequently to determine whether a particular bank's CRA Evaluation was in fact available and where it could be obtained. In addition, we found that there is broad national, as well as local, interest in the reports, but those not living in a bank's community could not readily find out whether a bank's report was available.

After considering this problem, the Federal Financial Institutions Examination Council voted at its December 7 meeting to recommend that each banking agency make public a regularly updated list of financial institutions examined by that agency for which CRA Evaluations are available. For all of you interested in obtaining CRA Evaluations for particular banks, the lists will take the guesswork out of the process.

Getting the Most Out of CRA

Prior to disclosure of CRA Evaluations, public interest in CRA was centered almost exclusively on two related issues. First, how well have financial institutions performed? Second, how vigorously have the banking agencies fulfilled their responsibilities? Those are valid questions, since they are the focus of CRA's primary legal obligations.

But I think that dealing only with those two issues obscures the most important question of all. And that is: How can we get the most out of CRA? And, the answer to that is not simple.

One reason is that there is at least one more very important element critical to the success of the CRA process and that's the role of the public (consumers, community groups, and others interested in community revitalization) and the part banks can play. These groups, including state and local governments, can be extremely important players in helping the CRA process work.

Certainly the banks must continue to take their CRA responsibilities seriously. Certainly we at the banking agencies must continue to pursue our responsibilities vigorously. And I can assure you that we at the Federal Reserve will.

But is that all there is to it? Not really.

Potential Roles for Community and Consumer Groups

Without strong and effective consumer and community group participation, I believe that CRA will never live up to its full potential.

We all recognize that community groups always have played a role in the CRA process. Through CRA-related public comments on banking applications -- commonly called CRA protests -- consumer and community groups have made their concerns about bank performance known. Local groups also have played important roles in helping structure effective programs that involve banks, and other public and private funds. They have shown time and again that they can bring their collective knowledge of local markets and programs to the table and help banks fashion appropriate responses to community needs.

But there are several other roles community groups can play. The first is effective use of the new CRA Evaluation disclosures. All of the regulations, all of the report preparation, and all of the procedures for public release, are not worth putting in place unless the disclosures are used constructively.

It is likely that all the judgments we make in CRA Evaluations will never totally satisfy either the banks or the community groups. Assessing CRA performance is, after all, in large measure, a subjective process and reasonable people can disagree. We expect some criticism of the public Evaluations and we will continue to do everything we can to improve the examination process, and ensure that the public CRA Evaluations are done well.

I think the real point of the CRA Evaluation exercise is to provide a mechanism to encourage public dialogue between financial institutions and their communities on how best to meet important community credit needs. I would hate to see the process bogged down in discussions with regulators as to whether a bank's public Evaluation and CRA rating was precisely correct. Although we value constructive criticism of our efforts, at some point the focus must turn to the business of the bank and the needs of its community. Otherwise, the focus is misplaced.

Instead, I would hope that both community groups and banks would be more inclined to use the CRA Evaluations as a jumping-off point for constructive discussions about what needs to be done in the community and how the banks might play a role. That goes for banks with "Outstanding" and "Satisfactory" CRA ratings as well as those rated "Needs to Improve" or worse.

In fact, I have been urging bankers that -- no matter how their CRA ratings come out -- they themselves might find it useful to publish their CRA Evaluations in local newspapers, along with their responses, to help stimulate dialogue. Of course, many banks with "Outstanding" performance ratings would <u>want</u> to publish their CRA Evaluations. But I think they should also consider including information on how they intend to maintain that performance in the face of changing community needs.

In my view, even banks rated "Needs to Improve" should not hesitate to publish their reports. Instead of being fearful about their reports, these banks should consider openly revealing them, along with any positive ideas they have about how the bank might proceed to address their CRA responsibilities going forward. They could also use that opportunity to specifically invite the community to provide its ideas on how the bank might improve its program and best target its activities to help meet the most pressing needs.

In other words, banks can turn the CRA Evaluation into a positive opportunity to open, or continue, dialogue with the community.

In using the CRA disclosure reports to begin or continue dialogue with banks, I also hope consumer and community groups will recognize several important factors which may shape discussions. One is that a CRA Evaluation of a bank is only an assessment of a bank's CRA performance. It is not, and should not be confused in any way with, the results of examinations we conduct focused on the safety and soundness of the bank. The CRA Evaluation is not an evaluation of the financial condition of an institution and should never be represented as such. This is a major concern of the banks and the banking agencies and I cannot overemphasize the importance of responsible action on this point. Consequently, we sincerely hope that community groups will play a positive role in helping the public understand the difference.

Another factor is that the CRA Evaluations and ratings are only snapshots in time. Each Evaluation report, in fact, includes specific introductory language explaining that the CRA rating is based on an examination conducted as of a certain date. Further, each report states that the Evaluation "does not reflect any CRA-related activities that may have been initiated or discontinued after completion of the examination."

Put simply, CRA performance is not static, while the Evaluation report produced by the bank's supervisory agency is only a measure of CRA performance at a moment in time. A bank may have taken quick action based on its CRA Evaluation, especially if it shows that the bank needs to improve its performance. On the other hand, a bank receiving an "Outstanding" or "Satisfactory" CRA rating may have changed its CRA program after release of the Evaluation and its rating may, therefore, no longer accurately reflect its record of performance.

The point here is that there is always room for dialogue and discussion with a bank, no matter what its latest CRA Rating might be. Community needs change just as a bank's CRA performance changes. Consequently, we expect banks to have an ongoing program for outreach and communication with their community. We would also hope that consumer and community groups would recognize the need to initiate constructive dialogue and discussion on community needs with banks on an ongoing basis. CRA Evaluations should not get in the way of that process.

A second role community groups can play, one that often helps stimulate dialogue, is continued use of the bank's Public Comment file. Consumer and community groups should not be reluctant to put their concerns and constructive suggestions about bank CRA performance in writing and send them to the bank. It is also useful to send copies of such letters to a bank's supervisory agency. Banks are required to put these letters and supporting information in a public comment file which is open to review by consumers and is used by regulators when they conduct CRA examinations.

Surprisingly, our examiners continue to report that they see few letters from consumer and community representatives in CRA

Public Comment files when conducting CRA examinations. We hope that consumers who do have concerns about a bank's CRA performance will write to the bank. Often such letters facilitate discussions with the banks and can result in development of responsive actions. They also help alert regulators to concerns in the community about a bank's CRA performance.

A third role community groups can play is in helping promote an accurate understanding of what CRA is and is not. As I noted earlier, CRA is not a charitable or giveaway program and it is not in anyone's best interest to foster this view. Dialogue between banks and uninformed members of the community based on this approach will probably not be very productive.

CRA-related lending is not a substitute for charitable contributions or for government programs. These funding sources provide the subsidies often necessary to structure effective financing that meets the needs of lower income communities. Subsidy, however, is not the function of private financial institutions, though their loans and investments may be combined with subsidy to produce affordable financing.

To the extent that CRA-related loans are really loans and not giveaways, CRA programs will have much wider support from the banking industry.

Fourth, and related, community groups can help play a constructive role by recognizing that economically unsound community lending programs are counterproductive in the long run. The long-term success of a program is much more important than short-term approaches designed to throw money at a problem. Long-term success is based on development of a sound plan, and appropriate loan products that meet both the needs of the community <u>and</u> the needs of the participating banks.

There are many examples of housing and neighborhood revitalization programs which have demonstrated delinquency and default rates equal to or better than a bank's conventional loan portfolios, while creating a real positive impact in the community. But that kind of success does not happen by accident. It requires good planning, respect for bank experience and use of sound underwriting guidelines.

No one has a bigger stake in building long-term support for CRA than consumer and community groups. To ensure that support, I believe that these groups must be in the forefront of those emphasizing the economic soundness of community development lending. A bank weakened by unsound community lending will be a weak partner for community groups in getting desirable results.

Fifth, in addition to helping plan sound programs, community groups have demonstrated that they are effective partners in implementing those programs as well. They can serve as a bridge for banks to neighborhoods. They can ensure that, once a program has begun, there is continuing community input so that adjustments can be made if necessary. Community groups can help market loan products that have been tailored to meet particular neighborhood needs and they can suggest effective bank advertising and outreach techniques. And some community groups can help develop clean loan packages for presentation to banks.

Finally, I would suggest that consumer and community groups, at both the national and local levels, have an important role to play in helping share CRA success stories. And by that I do not necessarily mean war stories about CRA protests.

I mean share with banks information on bank and community partnership programs that work: information based on experience with proven working partnerships among banks and their communities, and information about how government programs and various forms of subsidy can be used to help create good loan packages.

Many of our Reserve Banks are producing such information. Bank trade associations also have begun to develop case examples to share with their members. And many community groups have developed information-sharing networks that highlight effective approaches to community reinvestment. But I think you would agree that more needs to be done, and we need to work together to get the best result.

Conclusion

This is a very critical period for CRA. Its long-term viability as an effective means to foster community revitalization is being tested.

The effects of banking agency pressure, the disclosure of CRA Evaluations, and, yes, the honest enthusiasm of many banks have combined to result in a noticeable upturn in bank CRA activity. We have to make sure, however, that there is adequate capacity within the community to absorb on a sound basis the dollars and goodwill now being offered. I think community groups can play their most valuable role in helping banks identify good opportunities and develop successful lending programs.

I began this talk by saying that CRA was, in part, really a process that involves rights and responsibilities under law and relationships in our economy and banking system. It is a dynamic process that requires a cooperative effort involving financial institutions, banking agencies, local governments, and, equally important, consumer and community groups.

Financial institutions need to live up to their responsibilities and we as banking regulators will do our best to make sure that they do. We have put the legal apparatus and procedures in place. Now it is time to think much more about how we get the most out of CRA -- how we can best develop the long-term working relationships among banks and their communities that will guarantee successful reinvestment. They need to be partners, not adversaries. In a partnership, each party makes an investment and all share in the results, both good and bad.

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