Testimony of

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On behalf of the

Independent Community Bankers of America

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"Better Together: Examining the Unified Proposed Rule to Modernize the Community Reinvestment Act"

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Chairman Perlmutter, Ranking Member Luetkemeyer, and members of the Subcommittee, I am Quentin D. Leighty, CFO and President of First National Bank of Las Animas in Las Animas, Colorado. I testify today on behalf of the Independent Community Bankers of America where I am Chairman of the Policy Development Committee and a member of the Federal Delegate Board.

Thank you for the opportunity to testify at today's hearing, "Better Together: Examining the Unified Proposed Rule to Modify the Community Reinvestment Act."

The CRA was enacted in 1977 to ensure that banks serve the convenience and needs of their entire communities, including low and moderate-income (LMI) neighborhoods, consistent with safe and sound operation. This mission is the essence of what community banks do – inclusive and often customized lending in service of our entire communities, leaving no household behind. This explains community banks' outstanding and inclusive performance in Paycheck Protection Program (PPP) lending. Community banks made nearly 72 percent of the PPP loans to minority-owned small businesses and an even greater percentage of loans to businesses in lower-income and rural communities. CRA has not required us to shift or tailor our banking practices, but to document what we are already doing. This is true not only for my bank but for all community banks.

I am pleased to provide our perspective to this important discussion of CRA, the proposed inter-agency rule, and our suggestions for improving it.

Credit Unions Should Be Subject to CRA

I will note at the outset that, as is known to members of this committee, CRA does not apply to tax-exempt credit unions. This may have made sense in a former era when credit unions were subject to a strict common bond requirement and served limited populations. That era is long past. Modern credit unions are no longer subject to any meaningful common bond requirement. Community credit unions serve whole communities, and even common bond credit unions market their services broadly. Modern credit unions effectively operate as tax-exempt banks with near-equivalent powers. They have leveraged their tax exemption to grow larger and more complex and rapidly gain market share in retail and commercial lending as well as other financial services. We fully expect their expansion to continue unabated and transform the financial services marketplace. In the absence of CRA, credit unions are unaccountable for their service to LMIs, and enjoy a substantial regulatory advantage at the expense of consumers.

Moreover, the trend of credit union-community bank acquisitions has sharply increased in recent years, with increasingly larger community banks targeted for acquisition. When a community bank is acquired by a credit union, a CRA-covered institution is removed from the market with an adverse impact on LMI communities: Fewer institutions are held accountable for service to these communities and fewer consumers are protected by the robust consumer protection examination practices of the banking regulators.

ICBA and community banks urge this Committee to hold a hearing in the near future to examine the community impact of credit union-community bank acquisitions and the possible application of CRA to credit unions. These are urgent public policy issues and are ripe for the Committee's attention.

Our Story

First National Bank has a rich history of serving the communities of Southeast Colorado, tracing our roots back to 1901, when our region needed a local bank that understood the unique requirements, challenges, and values of its residents and businesses. Today, we are a $580 million community bank with 78 employees and 7 branches in three counties. Most of the communities we serve are low, moderate, and middle-income, and some are designated as either distressed, underserved, or both. We are the sole banking provider in two of the communities we serve, Las Animas and Ordway.

Our Experience with CRA

I am proud that my bank has consistently achieved CRA ratings of Outstanding. We are examined on a four-year cycle, and our last exam was completed in 2020. We have been examined as an Intermediate Small Bank since 2010, so we have recent experience as both a Small Bank and an ISB.

How do we account for our consistent Outstanding ratings? The answer is simply that we do what we have always done since long before there was a CRA, adhering to the core values and principles set forth in our mission statement. As a community bank, we are locally owned and operated by people with deep roots in the communities we serve. Our commitment is to meet the unique needs of our neighbors, guided by the traditional values we all share. This is reflected in our lending and donations of funds and employee time and expertise to organizations that are doing critical work in our communities.

First National Bank has two CRA assessment areas (AAs): Las Animas and Monument. As an ISB, we are subject to two tests, the Lending Test and the Community Development Test. In our 2020 exam, as in prior exams, we scored Outstanding in both of these categories. This score was based on:

- Our high average loan-to-deposit ratio of nearly 80 percent.
- The high percentage of loans, 70 percent, made within our AAs.

- The distribution of loans across census tracts within our AAs. Our results showed excellent penetration to borrowers of different income levels and businesses and farms of different sizes, particularly within distressed and underserved communities in the Las Animas AA.
- The examiners found no gaps in our lending pattern that would exclude low- or moderate-income communities.
- We demonstrated excellent responsiveness to the community development needs in each of our AAs. During the evaluation period, our bank provided 170 community development loans totaling over $16.3 million within our AAs. The loans helped provide 105 units of affordable housing to LMI families among other important investments. Further, our bank provided over $6.5 million in loans to promote economic stability through permanent job creation or retention in LMI and distressed middle-income geographies. We also provided over $800,000 in loan funds directed towards essential community services in LMI and distressed middle-income geographies.
- The bank provided 217 donations totaling over $172,000 within the designated AAs.
- In addition to lending and donations, a total of 27 bank employees and directors provided over 2,500 hours of community development services within the AAs.

Since the 2020 examination, we have continued and expanded our CRA activities and fully expect to receive a rating of Outstanding in our next exam.

I would like to share with you some recent examples of our activities that have made a real difference in our communities.

> In February 2021, First National Bank made a $2,885,000 loan with a reduced interest rate to Safe Passage to purchase and rehabilitate a building in a moderate-income tract area of Colorado Springs. Safe Passage is the Children's Advocacy Center for El Paso & Teller Counties serving more than 1,000 children and non-offending caregivers each year. They give abused children a voice and act as a single source of contact for medical, investigative, and legal services. In addition to Safe Passage, multiple community services are housed out of this building, including the Crimes Against Children Unit (CACU) of the Colorado Springs Police Department; KidPower, a non-profit organization that provides vital instruction to abused children and families on how to create and maintain safe emotional and physical boundaries; and the UC Health Memorial Health System, which partners with Safe Passage to provide onsite examinations in hospital-style rooms. The bank also made a $5,000 donation to Safe Passage.
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> Our employees serve on various boards in our communities. One of our loan officers currently uses his financial expertise to help several community organizations, serving on a high school Ag Education/Future Farmers of America advisory board, a housing and community development board, a resource center that provides crisis intervention, shelter, counseling, and support for victims of domestic violence, their children, and all

other victims of violent crime, and the local volunteer fire department as a trustee and fireman, helping with safety presentations for elementary kids. The bank has made loans to help the fire department obtain new vehicles, equipment, and build or expand stations. This year the bank made a $5,000 donation to help with an addition to their station.

First National Bank made nearly 900 SBA PPP (Paycheck Protection Program) loans totaling almost $42 million. One loan was made to a Hispanic woman-owned family restaurant that was required to close during part of the pandemic. The owner was able to continue paying her employees until they were allowed to reopen. Restrictions went from full closure to carry-out only before the restaurant was allowed to fully reopen. In addition, the bank purchased gift cards from various restaurants in our communities and gave them out to front-line workers (nurses, ambulance, fire, police) during the pandemic as a "Thank You" for continuing to serve in our communities.

Community Banks and CRA

First National Bank's commitment to our communities is replicated by thousands of community banks across the country. A typical community bank would have a similar list of community development projects that make a real impact in their communities. Many also choose to invest in MDIs and CDFIs that serve marginalized communities. But just as important as these high-profile projects and investments is a community bank's core lending to LMI families and small businesses in LMI census tracts that have been historically overlooked by the banking system.

As I noted earlier, CRA does not require a community bank to alter its activities or business model. A commitment to supporting our customers and communities across the diverse demographics we service is the essence of community banking. For this reason, nearly all community banks receive a CRA rating of Satisfactory or higher.

CRA Modernization Recommendations

In consultation with community banks from across the country, ICBA has developed the following CRA modernization recommendations.

<u>The Examination Process Should Be Clear, Consistent, and Timely</u>. Community banks experience inconsistencies in the examination process, which creates uncertainty and confusion. The inconsistent manner in which loans and services receive CRA credit occurs between examinations within an agency, as well as between agencies. This makes it incredibly difficult for community banks to plan and implement their CRA requirements responsibly. Agencies must adopt consistent definitions and qualifying activities criteria. Additionally, there is virtually no feedback during or following an examination until the actual performance evaluation is shared with the bank.

Asset Thresholds Should Be Adjusted to Reflect the Current Banking Environment. ICBA believes that the current thresholds defining “small,” “intermediate small,” and “large” banks for purposes of CRA performance tests do not adequately reflect the extensive consolidation and growth that has occurred in the industry since 1977 when CRA was adopted. The OCC’s 2020 final rule made a positive step by increasing the small bank threshold to $600 million and the intermediate small bank threshold to $2.5 billion. These changes are partially replicated in the interagency rule (discussed below). Updated thresholds would partially ease the CRA regulatory burden for most community banks without impairing agency assessment of CRA performance.

CRA-Qualifying Activities Should Be Expanded and Consistently Applied. ICBA supports a more forward-looking approach in qualifying activities for CRA credit by providing a CRA credit safe harbor for listed activities. An illustrative list was included in the OCC’s final rule and in the joint-agency rule (more below). While the qualifying activities list would not capture the entire universe of activities that would receive credit, it would provide banks with greater clarity.

Alternative Approaches for Minority and Women-Owned Financial Institutions and CDFIs. CRA regulations should exempt minority and women-owned financial institutions from documentation and full-scope examinations. ICBA believes it is appropriate for CRA to support such institutions through compliance relief as these are the very types of historically marginalized business that CRA is designed to support. For the same reason, ICBA supports accommodations for bank-designated, certified Community Development Financial Institutions (CDFIs), which provide credit predominantly to lower-income borrowers and communities that have been historically underserved. We also believe that there should be an incentive for all banks to enter into partnerships with MDIs, CDFIs, and women-owned financial institutions. An incentive could come in the form of a credit multiplier or impact score that would affect performance context.

Parity in the Application of CRA. I have already discussed the imperative of applying CRA to credit unions. By the same token, all financial service providers, including fintech companies and any financial firm that serves consumers and small businesses, should be committed to providing service to entire communities and should be subject to CRA. Branchless internet banks should be evaluated on a nationwide basis, with performance benchmarks that are at least equivalent to branch-based banks. An uneven playing field places community banks at a competitive disadvantage and inhibits their ability to serve their customers and their communities.

Current Agency Efforts

The regulatory agencies are in the process of modernizing CRA’s implementing regulations, which have not been updated since 1995. Since 2017, the Office of the Comptroller of the Currency (OCC), the Federal Deposit Insurance Corporation (FDIC) and the Federal Reserve Board of Governors (FRB) have worked to modernize the 1995 rule.

In June 2020, the OCC finalized a new CRA framework. That rule attempted to make performance evaluations strictly quantitative and to significantly change the definitions of qualifying activities. As noted above, the rule also raised the small bank asset threshold to $600 million and the ISB threshold to $2.5 billion. While the OCC's 2020 rule made several positive changes, it also imposed additional data collection burdens on community banks and did not include the FDIC or Federal Reserve Board, leading to a confusing and unequal regulatory landscape. Because of this, ICBA advocated for the rescission of the 2020 rule and urged the OCC to engage in a joint rulemaking with the FDIC and Fed. In December 2021, the OCC rescinded the 2020 rule, returning to its 1995 rule, which the FDIC and Fed also use. ICBA supported this decision because we believe there should be a unified, interagency rule.

The Joint Interagency Proposal

As you know, on May 5, 2022, the OCC, FDIC, and FRB released a proposed CRA rule that would create a modernized rule for the banking industry. Comments in response to the agency's notice of proposed rulemaking (NPR) are due on Aug. 5, 2022. ICBA is reviewing the proposal and conferring with community bankers and will submit a comment letter on behalf of community banks.

While we are not yet prepared to offer this committee a comprehensive, detailed response to the proposal, I will use this opportunity to make some preliminary observations.

Asset Thresholds

ICBA supports the threshold increases in the proposed rule, which are set forth below.

- Small Bank: The proposed small bank threshold is $600 million, an increase from the current level of $346 million.
- Intermediate Small Bank: The proposed ISB threshold is $2 billion, an increase from the current level of $1.384 billion.
- Large Banks: Banks with assets exceeding $10 billion would be subject to evaluation of digital and other delivery systems and deposit products and be subject to additional requirements

As discussed above, these threshold increases reflect industry consolidation and are appropriate to provide compliance relief for smaller community banks such as mine. First National Bank, currently an Intermediate Small Bank, would be categorized as a Small Bank, though we are approaching the proposed ISB threshold. The Small Bank designation would allow First National Bank and many other community banks in our asset range to direct more resources toward serving our communities. The proposed Intermediate Small Bank threshold of $2 billion is a welcome increase but falls short of our recommendation of $2.5 billion.

Small and Intermediate Small Bank Opt-In

Any change to CRA, even one that creates a more transparent method of evaluating banks, requires banks to completely overhaul their compliance management systems and retrain staff to comply with new requirements. For this reason, ICBA believes that small banks and ISBs should have the option to opt-in to any new CRA evaluation framework or continue to be evaluated under the status quo retail lending and community development tests.

The inter-agency proposal allows small banks (assets of less than $600 million) to be evaluated under the status quo small bank lending test or to opt into the new Retail Lending Test. ICBA strongly supports this approach which avoid disruptive change for banks such as mine.

Banks between $600 million and $2 billion in assets (ISBs) would be required to comply with the new Retail Lending Test but would have the option to retain the current community development test. This disruption comes at a high cost to community bank resources. ICBA recommends that ISBs retain the option of being evaluated under the status quo retail lending test.

Banks with assets exceeding $2 billion (large banks) would be required to comply with the new tests and would not have the option to retain their current exam framework. Many community banks have assets in excess of $2 billion, and as consolidation continues, more will exceed this threshold in the future. Adopting new CRA frameworks represents a substantial regulatory burden.

Assessment Areas

Small banks and ISBs would continue to be allowed to delineate facilities-based assessment areas including the portion of a county that the bank can be reasonably expected to serve, provided they continue to include only whole census tracts.

However, large banks would be required to delineate assessment areas that "consist of one or more MSAs or metropolitan divisions or one or more contiguous counties within an MSA, a metropolitan division, or the nonmetropolitan area of a state." This would be a change for large banks which are currently permitted to delineate portions of a county as a facility-based assessment area.

In addition to facility-based assessment areas, large banks would be required to delineate new retail lending assessment areas in geographies where they have a concentration of retail loan originations outside of their facility-based assessment areas. Only the Retail Lending Test would be applied in these assessment areas.

The agencies estimate that, using these thresholds, 104 large banks will be required to delineate at least one retail lending assessment area in a geography where they lack a physical branch.

Moreover, this proposed change will likely expand the number of geographic areas where branchless, internet-based banks are evaluated. However, as the agency estimates show, it will also likely impact some traditional, branch-based banks.

Out-of-Area Activities

As advocated by ICBA, the agencies' proposal grants credit for qualifying community development financing and services activities conducted beyond the boundaries of a bank's facility-based assessment areas. According to the proposal, banks "would receive consideration for qualifying activities anywhere in a state or multistate MSA in which they maintain a facility-based assessment area, when determining the conclusion for that state or multistate MSA. In addition, banks would receive consideration at the institution level for any qualifying activities conducted nationwide." This broader geographic consideration of community development financing will ensure that banks receive credit for the beneficial community development loans and investments they make outside the confines of their assessment areas

Qualifying Activities Confirmation and Illustrative List of Activities

ICBA strongly supports the proposal's requirement that the agencies maintain a publicly available illustrative, non-exhaustive list of activities eligible for CRA consideration. The proposal also creates a process for modifying the illustrative list of activities periodically. In addition, the agencies are proposing a process, open to banks, for confirming eligibility of qualifying community development activities. In this process, banks would submit the details of a potential loan or investment to their regulator and could receive a binding decision about whether the loan or investment would be eligible for CRA credit. ICBA strongly supports these changes as they would create more transparency and predictability in CRA evaluations.

Agency Data Confirm That Many Community Banks Would Fail the Proposed Retail Lending Test

The agencies' analysis of the new Retail Lending Test includes a table titled: "Distribution of Estimated Retail Lending Test Conclusions among Banks by Asset Size" and is based on banks that had a CRA examination that began in 2018 or 2019 and excluded Wholesale, Limited Purpose, and Strategic Plan banks. The table shows that 15 percent of banks below $600 million and included in the analysis are estimated to receive a rating of "Substantial Noncompliance" or "Needs to Improve" under the proposed new Retail Lending Test. An additional 24 percent of these banks would receive a rating of "Low Satisfactory." By contrast, fewer than one percent of

Federal Reserve and OCC evaluated banks received a less than satisfactory rating in 2018 and 2019, and only 1.7% of banks examined by the FDIC were rated as less than satisfactory.

Fortunately, as Small Banks, they would have the option of being evaluated under the current Retail Lending Test, but this data shows the magnitude of the change in the new Retail Lending Test.

The agencies estimate that 7 percent of Intermediate Banks and 7 percent of Large Banks would receive less than Satisfactory ratings. An additional 38 percent of ISBs and 41 percent of Large Banks would receive Low Satisfactory ratings. For these banks, the new Retail Lending test is not optional.

ICBA’s comment letter will contain recommendations for modifying the Retail Lending Test (as well as making it optional for ISBs) that will make it easier for banks to obtain ratings that reflect the significant LMI lending they do in their communities.

Conclusion

Thank you again for convening today’s hearing and for the opportunity to offer the community bank perspective on CRA modernization.

I’m happy to answer any questions you may have.