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<u>MEMO</u>

From: Kenneth H. Thomas, Ph.D.

To: Chair Jerome Powell & Vice Chair Lael Brainard via Docket No. R-1769 and RIN 7100-AG29;
Acting Comptroller of the Currency Michael Hsu via Docket ID: OCC-2022-0002; and,
Acting Chairman of the FDIC Martin J. Gruenberg via Docket No. RIN 3064-AF81

Date: August 5, 2022

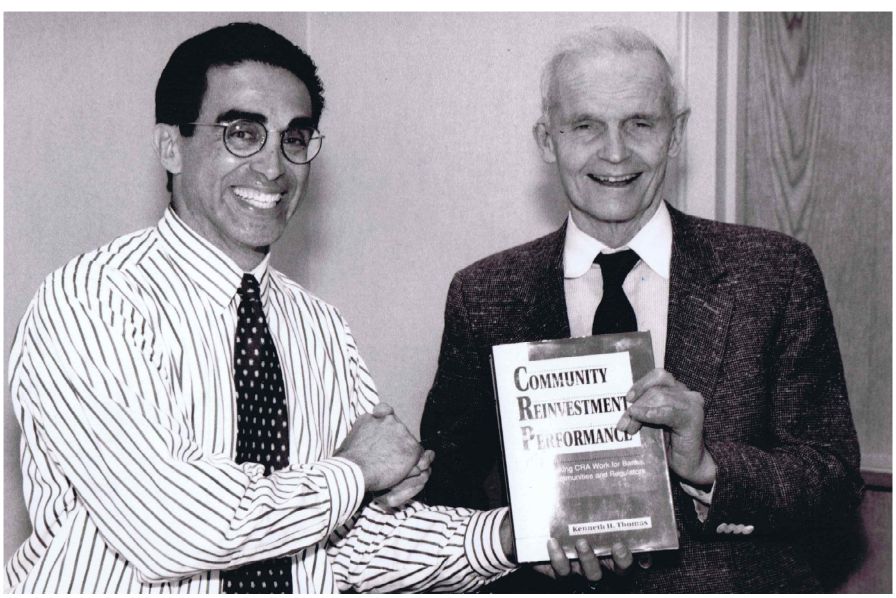
Re: Fourth CRA NPR Comment on "<u>The NPR Must Have the 5% Deposit Reinvestment Rule</u>"

This is my fourth comment on this NPR on CRA Reform, and it is titled *"The NPR Must Have the 5% Deposit Reinvestment Rule."* Before providing more details on this comment, I will first summarize my relevant background on CRA reform.

My comments represent my personal views and not those of any university, financial institution, company, or other organization with which I am or previously have been associated.

My Relevant Background on CRA Reform

My current and past expertise in CRA in general and its reform in particular are relevant to this comment. In short, I have spent the majority of my professional life since 1977 focused on the CRA. I was greatly honored to have known and spent time with former Senator William Proxmire, the "Father of CRA." The following photo was taken in 1995.



I am proud of the fact that my first book on CRA, Community Reinvestment Performance (Probus Publishing, Chicago, 1993), received the only endorsement he ever gave to any CRA publication:

> *Dr. Thomas' book, Community Reinvestment Performance, is far and away the best analysis of government regulation that I have seen in any field. He spotlights the regulatory problems that continue in CRA and points out precisely how they are being overcome. CRA will benefit enormously from this superlative examination and report.*

I have worked closely with numerous banks, community groups, and regulators on CRA since 1977, including training federal bank CRA examiners. Besides acting as a CRA consultant and being on the boards of various financial institutions, I am a cofounder and founder of two different CRA high impact mutual funds devoted primarily to providing CRA qualified investments to benefit LMI areas and people.

I had the privilege of testifying before Congress and federal bank regulators several times on CRA and related bank regulatory and public policy issues. Many of the recommendations in my books, including various CRA exam procedures and tests, were directly implemented into current bank regulations, and more details in this regard are found at www.CRAHandbook.com in The CRA Handbook (McGraw Hill, New York, 1998).

I was honored to receive the first "Award of Excellence" from the National Community Reinvestment Coalition (NCRC), along with Representative Joseph P. Kennedy and Comptroller Ludwig.

In summary, I have a vested interest in getting CRA reform "right," which I define as being what Senator Proxmire intended. We got it right in 1995 when I worked with Comptroller Ludwig and his OCC staff on the last major reform of CRA, and that is my goal during the present effort.

The 5% Deposit Reinvestment Rule Fix for CRA Modernization

As documented in a previous comment, modernization of CRA should be the one and only purpose of CRA reform, unlike the Fed's current NPR that makes it #2 of eight total objectives.

The previous NPR released by the OCC and FDIC is to be commended for making the 5% Deposit Reinvestment Rule a key part of their reform proposal. Although that NPR also went well beyond the modernization goal, it at least had the correct fix for the modernization goal of CRA reform.

This cannot be said for the Fed's current NPR, which is a very complicated solution in search of a problem. The Fed clearly understood the need to consider how Assessment Areas must be changed for branchless and other banks obtaining deposits from distant markets with little to no CRA reinvestment of those deposits.

However, like much of their monetary policy, the Fed came up with the wrong answer. The Fed in both the current NPR and its previous ANPR got this totally backwards by focusing on where branchless banks make loans rather than where they get their deposits.

The one and only correct fix for CRA modernization is to focus on deposits because the intent (and middle name) of the Community Reinvestment Act is REINVESTMENT of DEPOSITS.

In fact, I once asked Senator Proxmire why he named this law as he did, and his answer was very clear that the purpose of CRA is to reinvest deposits back into their entire sourced communities including LMI areas.

The 5% Deposit Reinvestment Rule that was included in the previous joint Notice of Proposed Rulemaking by the OCC and FDIC was a variation of a previous reform concept to require banks obtaining deposits from outside their headquarters community to benefit the areas sourcing those deposits. This reform is more important than ever now with so many fintechs and other giant tech barbarians like Google and Amazon lining up outside the banking gate.

The previous proposal would require all banks with 5% or more of their deposits in any area to reinvest a commensurate portion of their CRA benefits there. The OCC and FDIC's NPR limited this 5% Deposit Reinvestment Rule to banks with more than half their deposits from outside their current facility-based Assessment Area without requiring any commensurate CRA benefit. However, they at least focused on deposits instead of the Fed inappropriately focusing on loans.

Eliminating "Carpetbagger Banks"

Under the current regs, branchless banks can place up to 100% of their CRA benefits in their home office community where they have a physical presence. In the case of credit card banks, the primary beneficiaries are three "sanctuary states," namely Delaware, South Dakota, and Utah that provide a safe harbor with favorable state usury ceilings.

As a result, tens of billions of dollars of community development (CD) loans and investments and tens of thousands of hours of CD services have benefited Wilmington, Sioux Falls, and Salt Lake City rather than our large MSAs sourcing their deposits like New York, Chicago, LA, Dallas, and Houston. Despite containing less than 2% of the nation's population, these three sanctuary states are reaping nearly 100% of the CRA benefits primarily sourced by our large MSAs.

This huge misallocation of CRA resources is inconsistent with Senator Proxmire's Community *Reinvestment* Act, where he intended that federally-insured deposits be *reinvested* back into their community rather than some credit card-friendly city a few thousand miles away.

The best example of this problem is my hometown of Miami, part of the nation's seventh largest metro area, with 40% of the deposits of the third largest state. My previous concern over what I called "carpetbagger banks", which come to this deposit-rich state to harvest seniors' savings to lend elsewhere, was mainly directed toward the giant banks that now dominate Florida like Bank of America and Wells Fargo with a combined one-third market share.

This has changed somewhat in recent years where many out-of-state regional banks have bought Florida's local banks and are doing a better job of reinvesting in local communities than interstate giants like Bank of America and Wells Fargo.

Some of this improvement in local lending, however, is the result of the federal law monitoring nonlocal loan-to-deposit ratios for interstate branch banks. Unfortunately, neither this law (The Riegle-Neal Interstate Banking and Branching Efficiency Act of 1994) nor CRA do anything to prevent credit card and other branchless banks from taking local deposits and reinvesting them elsewhere as is currently being done.

Synchrony Bank's Siphoning of South Florida Deposits to Benefit Salt Lake City

Consider, for example, the roughly $100 billion Synchrony Bank, formerly GE Capital Retail Bank, the nation's sixth largest credit card issuer, with reported deposits in its Salt Lake City area main office.

Like many other credit card banks, it regularly advertises its above-market deposit rates in South Florida media. It is reasonable to assume that with this targeted advertising in an MSA with 2% of the nation's population and even greater share of its wealth that at least 5% of that bank's deposits come from South Florida.

Synchrony Bank's most recent CRA exam as of December 31, 2018 reported $464 million of CD investments and $548 million of CD loans totaling more than $1 billion benefiting their home Salt Lake City Assessment Area within its most recent three-year review period. There was an additional $250 million of CD investments benefiting undisclosed outlying areas for a grand total of $1.25 billion of CRA benefits, representing more than 1% of their deposits.

There is no public information on the portion of their deposits emanating from their home Salt Lake City MSA, but we do know that the entire Salt Lake City MSA and state of Utah represent just 0.4% and 1.0%, respectively, of the nation's population.

Under the proposed 5% Deposit Reinvestment Rule for such banks, assuming at least 5% of Synchrony Bank's deposits come from the Miami MSA, they would be required to reinvest at least 5% of their reported $1.25 billion of CRA benefits or a total of $62.5 million here.

There is a critical need for such funds considering that Miami is Ground Zero for the nation's affordable housing crisis, especially with the large number of Wall Streeters and other One Percenters relocating to South Florida during and after the Pandemic.

While that bank may deserve its Outstanding CRA rating for their performance in the Salt Lake City MSA, this is certainly not the case for the Miami MSA and other large ones being targeted by these banks and getting little to nothing in return for financing their credit card operations.

For example, the New York MSA, with 6% or our nation's population and even greater share of wealth, probably represents around 10% of that bank's deposits. Assuming that is the case, this proposal would have entitled New York to at least $125 million in CRA benefits from Synchrony Bank over that same period, and those funds could have helped New York's huge affordable housing and homeless problem.

Three Sanctuary States Are Receiving Disproportionate CRA Benefits

Most of the largest credit card banks plus many other internet and branchless banks are based in one of the three credit card "sanctuary" states providing favorable usury laws. With just 1.6% of our population and 1.7% of our businesses, these three states together represent a whopping $1.9 trillion in deposits or 11% of all FDIC-insured deposits as of June 30, 2021. In fact, Utah ranks 5th, South Dakota ranks 6th, and Delaware ranks 11th in terms of total deposits despite their respective population rankings of 30^{th,} 46th and 45th.

With fewer than 2% of the nation's population and businesses in these three states, it is reasonable to assume as much as 95% of their reported deposits or $1.8 trillion originate from other states. Assuming roughly 1% of deposits of these banks are used for CRA loans and investments, which is not unusual for many credit card banks, this would mean that as much as $20 billion would be regularly reinvested in our large cities rather than these three credit card sanctuaries.

To put this into perspective, the OCC recently estimated that all banks provided $482 billion of CRA (community development and non-community development) lending in 2017, representing some 4.1% of bank deposits.

The 5% Deposit Reinvestment Rule would not impose an undue regulatory burden, since it is standard operating procedure for branchless banks to geocode their deposits at least down to the zip code level. In fact, a senior officer of one such very large credit card bank told me that they would have a CRA responsibility in about seven major MSAs (including Miami and New York) as a result of the 5% Deposit Reinvestment Rule instead of their home MSA.

Also, these branchless banks would now have many more CD options around the country, instead of competing with other giant banks for limited opportunities in those sanctuary states. Moreover, community banks there would likewise benefit, since they often find it difficult to compete for CRA credits with the giant branchless banks headquartered there.

Our Forgotten Cities like Miami deserve their fair share of CRA benefits from the credit card, internet and other branchless banks that target them for funding, but this will happen only if they are required to proportionally reinvest their deposits in the spirit of CRA as originally proposed with the 5% Deposit Reinvestment Rule.

The Fed's NPR Benefits Branchless Banks

The giant branchless banks that would be impacted by the variant of the 5% Deposit Reinvestment Rule in the OCC/FDIC Joint NPR cleverly convinced friendly regulators, industry and community groups that it would increase CRA "hot spots" to the disadvantage of CRA "deserts," since most of their deposits come from metro areas.

This is a blatant misrepresentation of this rule, which requires deposits from rich neighborhoods (or hot spots) in big cities be reinvested in poor neighborhoods (or deserts) *in those same cities.* Call it a "Robin Hood Rule," where deposits from the rich in our big cities benefit their poor.

For example, the tens of billions of deposits in branchless banks coming from South Florida's affluent hot spots like Coral Gables and Pinecrest would now be reinvested in distressed deserts like Liberty City and Little Haiti. Who could argue with such needed reinvestment, other than "carpetbagger" banks and their home states like Delaware, South Dakota, and Utah currently benefiting from South Florida's deposits?

Branchless banks also disingenuously cited a data burden, even though they geocode deposits down to the zip code and smaller level. Deposits are the raw material of banking, and every good banker knows the geographic source of their deposits. Any banker who does not know the geographic source of their bank's deposits, their basic input or raw material, should not be in banking.

The current NPR adopted the Fed's previously suggested approach of essentially allowing branchless banks to place their CRA benefits *anywhere in the nation*. Even worse is the backwards suggestion of evaluating branchless banks' CRA performance in areas where they make *loans* rather than source deposits.

This distorted view of a Retail Lending Assessment Area (instead of the OCC's deposit-based one) is contrary to the letter and intent of CRA. Also, it encourages bad public policy if a bank is only lending in affluent communities and redlining distressed ones sourcing deposits.

For this reason, the branchless banks will not be required to reinvest into their sourced deposit communities under the current NPR but can continue their current practice of lending wherever they are or want, since a lending based Assessment Area is based on their lending.

Thus, the Fed's NPR not only protects branchless banks from having to evaluate and meet credit needs in local deposit sourcing communities but also allows them to continue their current carpetbagging practices to the detriment of Forgotten Cities like my hometown of Miami.