Remarks by

Ellen Seidman
Director, Office of Thrift Supervision

Before the
National Community Reinvestment Coalition
Western Regional Conference

on the Topic of
Communities: Commitment, Reinvestment, and Development

December 5, 1997
San Diego, California

Five weeks ago, in my first official appearance as the Director of OTS, I spoke to the American League of Financial Institutions in Los Angeles. Since then, I have had the opportunity to speak to numerous other people about the community development activities of thrift institutions.

What I have found, of course, is that the level of involvement of financial institutions in their communities is mixed. But, I have also found that, of the institutions that are significantly engaged, many have developed effective business strategies with a community focus that have proven to be quite successful -- and profitable. It is these types of programs that I believe offer the greatest opportunities for future success -- and to which I will direct the bulk of my remarks today.

I will also talk about our efforts to implement the new CRA regulation and the challenges we are facing. Finally, I will offer some remarks about the OTS Community Affairs Program.

Current Realities and Future Challenges

Despite the controversy that CRA has generated over the past several years, its success cannot be refuted. CRA has helped focus the lending activities of insured depository institutions on rebuilding their communities and promoting economic revitalization. Unfortunately, many communities still struggle with unemployment, the impact of welfare reform, inadequate housing and educational access, and poor public services. Mobilizing private and public sector resources to address these problems takes real commitment.

Financial institutions and the communities they serve must depend on each other to thrive, as well as to effect meaningful change. If disconnected from their communities, financial institutions will inevitably find themselves with no community to serve. But, as you know well, partnerships that include financial institutions, businesses, communities, local governments and non-profit organizations have the power to revitalize neighborhoods and stimulate job creation, economic and business development, and improvements in infrastructure and support services.

Although there is no particular formula for the success of these partnerships, two aspects of their operations bear notice. First, the contributions of financial institutions that focus on housing-related credit and investment are critical. Second, those financial institutions that provide business capital both foster improvements in the level of community services and create jobs.

Thrifts have long been providers of housing loans. They now have increased authority for small business lending. This permits thrifts to have an increasing impact in their communities by being able to respond to a wider range of credit needs. Financial institutions that use the flexibility of their lending powers to advance community change can be catalysts for successful community development efforts.

The Current Landscape

The intense competition among financial service providers, both in general and to meet their CRA obligations, has increased the availability of financial services in some otherwise underserved market areas. This competition benefits low- and moderate- income individuals by driving down prices and thereby creating greater opportunities for more people. Unfortunately, as competition increases in local market areas, institutions that have partnered with communities from the start -- particularly small, community-based financial institutions -- may find it harder to compete with larger, regional or national firms that have lower cost structures, and prices for the products they offer.

Notwithstanding the availability of less costly financial products from larger providers, a concern is that some of these lenders may be out of touch with community needs so that, in the long run, communities could be damaged if local banks and thrifts are driven out of business by larger lenders. On the other hand, the contributions that large institutions make to community reinvestment are often extraordinary in terms of dollars, creativity, and commitment.

Clearly, there is room for community-based institutions, as well as large, nationally-oriented lenders to promote community-based lending programs. Optimally, these institutions will work together to effectuate meaningful change and community improvement. Strategic alliances and partnerships between institutions that already have a presence in a community and outsiders that have significant capital resources available for community lending activities can produce a win-win situation for both. It is important, however, that these alliances work in concert with local community organizations and government officials to create useful programs.

Most of you in this room have had experience with some of the venerable old partnerships that have served this area, such as SAMCO, the Savings Associations Mortgage Company. But there are other similar organizations. For example:

- In Washington State, the Washington Community Reinvestment Association is a coalition of less than a dozen thrifts, with asset sizes ranging from $200 million to $25 billion. WCRA, with an original pool of $75 million, specializes in affordable home lending by partnering with government agencies and other nonprofit housing groups to leverage its funds and make properties throughout the state more affordable. For participating lenders, WCRA provides a risk-sharing vehicle for the financing of low-income housing units; a trusted and reliable investment source, particularly for smaller thrifts; and a concentration of affordable housing expertise.

- In Montana, the Glacier Affordable Housing Foundation, working with commissioners from 5 different counties, 3 financial institutions, and several federal and local agencies, assists first-time home buyers dealing with the escalating cost of housing attributable to migration into the state. The nonprofit foundation has established recyclable grant funds of $1.7 million to assist residents of the 5 predominantly rural counties. Collectively, the counties are able to access Federal HOME and Community Development block grant funds, and the Foundation was able to secure an Affordable Housing Program grant from the Federal Home Loan Bank of Seattle.

Implementation Issues Under the Revised CRA Regulation

<u>The New CRA Regulation.</u> Let me report briefly on our progress in implementing the new CRA regulation. Small institutions have been subject to the new rule since January 1996, and the rule kicked in for large institutions this past July 1.

Meeting community credit needs is, of course, at the heart of the CRA and the new regulation. Given this focus, it is essential that the agencies properly implement the new rules. So far, I am encouraged. Nonetheless, some community organizations have looked at the ratings assigned by the agencies -- particularly for large institutions that opted in early under the rule -- and are concerned that too many received top ratings out of the box.

While I will not minimize these concerns, a few observations are relevant in understanding the ratings. The ratings distribution is based on a very limited sample of institutions that carefully self-selected their evaluation method. Many of these institutions had maintained satisfactory or better CRA performance for years. Moreover, this group of institutions appears to have placed a particular priority on their CRA obligation and on meeting the credit needs of their communities.

I think it is important to focus not just on how many institutions fall into various ratings categories under the new rules, but also on whether we are applying the CRA rules in the way they are intended. The rules are intended to spur and recognize both the innovative and consistent provision of financial services in our communities, while encouraging continuous improvement by financial institutions. Critical to this analysis is whether we are measuring compliance and performance consistently, not only among similarly-situated institutions, but across regional and agency lines.

The OTS, along with the other banking agencies, is taking several steps to ensure consistency and accuracy in measuring CRA compliance. First, the agencies will soon be conducting CRA examinations jointly in a number of institutions so we can learn how each agency s examiners are interpreting and applying the rules. I believe this will improve the consistency of our approach.

Next, the banking agencies are reviewing examiners public evaluations of large institutions to determine whether the information is understandable, to ensure that examiners are using the correct facts and data to support their conclusions, and to review consistency among the agencies. Upon the completion of this and the preceding joint agency examination projects, the agencies will conduct additional interagency training for examiners, focusing principally on areas where the process can be improved.

Finally, the agencies are in the process of scheduling meetings in the upcoming months with community organizations and industry participants to discuss specific implementation issues that have arisen under the new CRA regulation.

We currently have an opportunity, at this stage of implementation of the CRA rule, to ensure that we are on the right track. These initiatives, coupled with existing interagency efforts to ensure consistency -- including interagency interpretive letters and a CRA Question and Answer publication -- should help considerably in the banking agencies efforts to retain the CRA focus on meeting community credit needs.

OTS Application Processing Rules. In April, as part of OTS ongoing efforts to streamline its rules and regulations, a proposed revision of our applications processing rule was published. Several of you raised concerns about the proposal -- relating primarily to the time available for protests and the availability of oral argument on a protest.

I am pleased to announce that, just yesterday, the OTS published a revised applications processing rule that retains the oral argument feature of our rules while providing more structured opportunities for informal resolution of issues. Oral argument will be available in the event that informal meetings between an applicant, one or more commenters, and the agency fail to resolve issues raised by the commenters in written submissions to the agency. We also extended the comment period from 10 days after public notice (with a possible 7-day extension) to 25 days after filing. The applicant may publish notice up to seven days before filing. In addition, we now publish timely notice of all new application filings on our web page, in a special Significant New Applications section. This page is updated daily.

I believe these changes strike the proper balance in addressing the concerns of applicants and the community in ensuring a full and fair airing of all issues, including CRA issues, raised in connection with a pending application, while also not unduly delaying OTS consideration of pending applications.

Emerging CRA Issues. A matter that has attracted significant attention recently involves institutions offering products and services in nontraditional ways. For example, some financial institutions are using the mail and telephone to reach new markets, while others are utilizing electronic means, such as the Internet. Perhaps most interesting are the institutions that have affiliations with other financial services providers, such as insurance and securities firms, that can utilize the delivery channels from these other existing businesses to provide banking products and services. In some instances, these nontraditional methods are employed on a national basis without local offices. This approach raises significant challenges in applying CRA.

So far, we have addressed these issues on a case-by-case basis to ensure that the implications of these methods are responsibly considered as part of a comprehensive CRA plan. For example, as part of its recent application for a thrift charter, the Travelers Group recognized that its CRA obligation did not simply end with a strong commitment to the local community where its thrift will have an office, but that it extended to all the communities where it intends to make loans. In connection with its application, Travelers committed to expand its internal controls to assure ethical practices and compliance with consumer protection and fair lending laws, and to make at least $430 million in home equity loans to low- and moderate-income borrowers over the next three years. They also committed to a special compliance program designed to protect consumers of high loan-to-value or high-cost home equity loans and not to discriminate in lending because of age or location of the dwelling. We expect other applicants to make similar commitments, consistent with their business plans.

Although our case-by-case approach provides the most workable method for addressing CRA issues for now, we must seek to clarify more generally how CRA obligations will be met in nontraditional banks and thrifts in the future. We are currently working at the interagency level to do just that.

In addition, I believe there is merit in pursuing a best practices approach. This could be achieved by having financial services providers work with the banking agencies and community groups to develop a model or a set of operating principles that recognize how those who do community reinvestment best, in all dimensions, meet the challenge.

Enhancing our Community Affairs Efforts

Another important aspect of our efforts to encourage responsible community development initiatives is our Community Affairs Program. The program is designed to promote sound community investment by OTS-regulated institutions. Significantly, when the program was established four years ago, the OTS was in the midst of an overall downsizing of its staff. Despite the agency s downsizing, the Community Affairs Program was implemented. I think this is evidence of the agency s strong commitment to this program.

Over the past four years, the individuals involved in our Community Affairs Program have concentrated their attention at the grass roots level, forging relationships with individual thrifts, local governments and community groups in their regions. Given the limited resources of the agency over this period, the accomplishments of this program are impressive.

During 1998, in addition to enhancing our community outreach efforts, we will concentrate on four new initiatives. These involve urban home ownership, rural development, lending on tribal lands, and welfare reform. In pursuing these initiatives, we are fortunate to have the assistance of three individuals with hands-on community development experience who joined us as part of the agency s Regulatory Fellows Program. In addition to assisting our existing Community Affairs staff, we anticipate that these individuals will share with us ideas for improving the way we do our business, and help us evaluate our role from a community-based perspective.

Concluding Remarks

The OTS is committed to assisting communities and thrifts in rebuilding our neighborhoods and revitalizing our communities. However, success can only be achieved through a sincere and concerted effort by all parties involved in the process -- communities, government, financial institutions, businesses, individuals and non-profit organizations. Partnerships that include all of these players appear to offer the greatest opportunities for pursuing viable community development programs.

The OTS is committed to serving as an intermediary in developing these partnerships. Through our outreach efforts, educational forums, written guidance, and examination function, we can fulfill our role by gathering and sharing information, by fostering community partnerships and capacity-building, and by encouraging thrifts to be all they can be in and with their communities.

Although there are limits to what any one group can do, there are no limits to what we can achieve when our strengths are combined. We all have the responsibility to develop and implement innovative and creative solutions to problems facing both rural and urban communities and their residents. The potential I see from leveraging the attributes of many is boundless. I accept OTS part of the challenge, and look forward to working with you as you pursue your efforts in this process.