



A Next System of Community Investment:

# COMMUNITY REINVESTMENT ACT REFORM IN THE 21ST CENTURY

*By Devin Case-Ruchala*



THE NEXT SYSTEM PROJECT



# A next system of community investment: Community Reinvestment Act reform in the 21st century

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## About this report

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Since 1977, the Community Reinvestment Act (CRA) has required banks in the United States to take affirmative steps toward meeting the credit needs of the communities in which they operate, including low- and moderate-income neighborhoods. In 2018, the Office of the Comptroller of the Currency requested public comment on proposed reforms that could make significant changes to how the CRA is administered.

This working paper is intended to inform and guide responses to the OCC proposed rulemaking notice as well as a longer-term reform agenda that could lead to a “next system” of banking and investment that better serves the credit and development needs of communities. This agenda aims to align the CRA with community wealth building approaches and assert a more fundamental public purpose obligation for financial institutions. The regulatory and legislative reforms proposed in the working paper address broader changes within the financial services industry and critical assessments of the law’s effectiveness in the communities that it is intended to serve.

## About the author

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**Devin Case-Ruchala** is a graduate student at the University of North Carolina at Chapel Hill, pursuing a political science doctorate in the political economy of finance. Devin has a background in the cooperative sector, including several years served as treasurer and board member of a 50-member housing cooperative in Bloomington, Indiana, and work with Shared Capital Cooperative, a national cooperative loan fund and community development financial institution (CDFI).

# Introduction: CRA and the need for system change

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In late March 2017, the Office of the Comptroller of the Currency (OCC) released its results of an examination into Wells Fargo Bank's compliance with a law called the Community Reinvestment Act (CRA). The CRA, initially signed into law in 1977, requires that banks lend and invest in the communities where they have deposit-taking branches. The report examined Wells Fargo's "record of meeting the credit needs of its entire community, including low- and moderate-income neighborhoods, consistent with the safe and sound operation of the institution" between November 2009 and November 2012.

The results of the assessment are worth reviewing because for newcomers to the CRA it highlights some incongruities of the legislation in the modern banking context (whereby some banks, particularly the largest banks, are simultaneously key providers of a significant amount of community capital but also a force stripping capital from communities and perpetuating inequities in access to capital).

The examiners write:

The bank's overall CRA Performance Evaluation rating was lowered from "Outstanding" [as awarded in 2008] to "Needs to Improve" as a result of the extent and egregious nature of the evidence of discriminatory and illegal credit practices...The findings reflect an exten-

sive and pervasive pattern and practice of violations across multiple lines of business within the bank, resulting in significant harm to a large numbers of consumers. The bank failed to implement an effective compliance risk management program designed to properly prevent, identify, and correct violations. Further, bank management instituted policies, procedures, and performance standards that contributed to several of the violations for which evidence has been identified.<sup>1</sup>

Immediately above this text is a table indicating that, aside from these "egregious" practices with regards to "fair lending and other illegal credit practices," Wells Fargo was awarded an "Outstanding" rating for its "Lending" and "Investment" activities, and a "High Satisfactory" rating for its "Service" activities. That is, it received an "Outstanding" and "High Satisfactory" rating for its lending, investing, and service activities to the "entire communities" surrounding its branches, including low- and moderate-income neighborhoods (emphasis added).

On a purely intuitive level, without going into the history or detail on the mechanisms of the CRA and

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1 Office of the Comptroller of the Currency. "Community Reinvestment Act Performance Evaluation: Wells Fargo Bank, National Association." September 30, 2012. The OCC is the federal financial supervisory agency responsible for reviewing the performance of nationally chartered banks in meeting CRA requirements.

Performance Levels	Wells Fargo Bank, National Association Performance Tests		
	Lending Test*	Investment Test	Service Test
<b>Outstanding</b>	X	X	
<b>High Satisfactory</b>			X
<b>Low Satisfactory</b>			
<b>Needs to Improve</b>			
<b>Substantial Noncompliance</b>			

\* The Lending Test is weighted more heavily than the Investment and Service Tests when arriving at an overall rating.

A chart from the 2005 examination of Wells Fargo’s compliance with the Community Reinvestment Act.

its exam ratings, these results seem in conflict with one another. First, we may ask, how it is that Wells Fargo used “egregious” discriminatory and illegal credit practices that resulted in “significant harm to large numbers of consumers,” but also did an “outstanding” job at meeting the credit needs of the communities where it operates? Moreover, how does “an extensive and pervasive pattern and practice of violations... resulting in significant harm to large numbers of consumers” not amount to a rating of “substantial noncompliance”? Lastly, how useful is a report dated September 30, 2012, but only released in 2017?

The technical explanation with regards to the first of these questions is that the CRA exams first evaluate financial institutions on the basis of their lending, investing, and services provisions, and then provide an additional review of fair lending practices to test for discrimination on the basis of race or gender. Poor performance on this corollary test can result in a downgrade in the rating of the overall test. In this case, Wells Fargo was downgraded for price discrimination, meaning it may have done an “outstanding” job lending to low or-moderate communities, but simultaneously discriminated on the basis of race.<sup>2</sup>

2 Horowitz, Ben. “Fair lending laws and the CRA: Complementary tools for increasing equitable access to credit.” *Federal Reserve Bank of Minneapolis*. March 8, 2018. <https://minneapolisfed.org/publications/community-dividend/fair-lending-laws-and-the-cra-complementary-tools-for-increasing-equitable-access-to-credit>.

Still, this technical response, which is not made particularly clear in the remaining 1,200 pages of the exam report, does little to explain the more fundamental logical incongruities of this exam result. Given that the lending exam is intended to assess Wells Fargo’s performance in lending to the *entire* communities in its assessment area and given that Wells Fargo engaged in discriminatory lending practices, how does it manage receive a rating of “outstanding” in the first place? And still we are left with the question of how such practices result in a rating of “needs to improve” and not “substantial noncompliance”? What’s more, the sole repercussion for Wells Fargo’s CRA exam rating is that an application for a merger or expansion through a new branch may be denied. No fines, revoking of existing privileges, or any other punitive penalties may be assigned, outside of what may result from separately filed class action lawsuits related to its “discriminatory and illegal credit practices.”

The outcome of Wells Fargo’s exam is perhaps unsurprising. It fits neatly into the now-prominent narrative that has emerged in the 10 years since the 2007-2008 financial crisis of “big banks” favoring short-term profit gains via whatever means possible rather than supporting equitable and sustained social and economic welfare (and long-term financial and economic stability). However, using Wells Fargo’s exam results as an example here is not to single out that

particular bank as a folk-devil, an easily identifiable entity to offload blame about the nation's economic ills, including growing income inequality, recurring economic crisis, increasing concentration of wealth, persistent racial wealth gaps, stagnant wage growth, and growing employment precarity. Rather, it illustrates the role major banks can, and all too often do, play at a systemic level in perpetuating and exacerbating these economic ills, at the same time that they direct billions of dollars into communities under the guidance of the CRA.

The incongruities evident in the exam results (and Wells Fargo's behavior) further highlight the challenges facing contemporary public policy to holistically assess and reform the behavior of major economic institutions. In this instance, the simultaneously "egregious" and "outstanding" actions of Wells Fargo are a telling contradiction at the heart of the present political economic paradigm in which large financial institutions predominate; that is, the purported freedom of individuals and small businesses to consume and engage in free enterprise is often constrained by the continual extraction of wealth and resources by large financial institutions, either by discriminatory and exploitative lending practices or by speculative lending and investing activities that bring about economic instability and recurrent financial crises.

This dynamic, of course, is not the fault of the CRA per se, nor would an adjustment to the CRA evaluation criteria alone necessarily resolve such contradictions as large financial institutions being both the force of the creation and destruction of capital, and serving as both an opportunity and barrier to capital access. In fact, if anything the CRA can be credited for motivating the better half of the contradiction, in that its primary function has been and continues to be requiring that banks redirect some portion of their assets toward loans, investments and services in low- and moderate-income communities. Given the sheer size of the banking industry today, this means hundreds of billions of dollars being redirected back into low- and moderate-income communities that presumably would not occur were it not for the CRA.

**The CRA is critically important for funneling capital back into marginalized communities. But as the CRA has grown increasingly necessary, so has the need for reform.**

However, the other half of the contradiction persists due to, among other factors, weak enforcement mechanisms, gaps in the examination process, and changes in the structure of the financial system since the CRA was first enacted in 1977. This has led to increasing and widespread agreement in recent years that the CRA is overdue for an update.

This working paper builds on such calls for reform by acknowledging the CRA's past successes and echoing calls for reform within the current regulatory framework. It also takes a step back to consider how the CRA fits into the broader political economic system and assess the extent to which it can be improved upon and made a better tool to support community investment in the 21st century. The paper details the evolution of the CRA, explains its current context, and puts forward a sample policy reform agenda for the 2020s that considers reforms within the current regulatory framework of the CRA as well as community investment legislation and alternative financial institutions outside the CRA that may help address community financing needs in a more holistic way than reliance on major banks.

A brief overview of the structural and ideological barriers to system-changing reform (considered in Part 2 of the paper) also indicates the pressing need in the 21st century for further interrogation of the most fundamental assumptions around the relationship between the government and the market in the United States if the CRA is to be extended beyond deposit-taking institutions, and if federal economic policies more generally are expected to play an effective role in addressing the country's most endemic social issues.

These barriers to system change are understood and felt the most in many communities left behind by the current system or who see the threats to equitable and sustainable wealth building and to local ecologies that the system imposes. Consequently, signs of a new political economic system are already emerging as local communities—exploited, excluded, or pushed to the margin—have begun experimenting with a wide range of innovative institutions, approaches, and policies.

In recent years, The Democracy Collaborative (TDC), among others, has begun to collect and highlight some of these examples of how the groundwork for a next system is already being developed in local “laboratories of democracy” through its framework of “community wealth building”—an asset-based alternative to traditional extractive models of economic development. Building community wealth, in this sense, means more than just income or growth, but the shared ownership and control of assets and the economic security afforded through this collective ownership. Through its Next System Project, TDC has started to link the strategies, approaches, and institutions of community wealth building with a vision of a “next system” that is more cooperative, equitable, and ecologically sustainable, in which the ownership of assets is democratized at every level.

This working paper builds on this work by also considering the CRA—its evolution, present context, and proposals for reform—in the context of community wealth building and system change. It does so by first considering the historical context of the CRA’s past successes and tracing the specific developments in the banking industry that subsequently have increased the need to reform the CRA to improve its applicability and efficacy—namely increasing financialization of the banking sector and movement away from deposit-taking branches. It then considers how the CRA in its current regulatory framework, which puts forward definitions and criteria of what qualifies as “community development” projects, can be built upon to include more community wealth building approaches. The imperative of such additions, as well as

the reforms forwarded in other calls for modernizing and improving the CRA, is evidenced through an examination of the shortcomings of the CRA’s current criteria, evaluation, and enforcement mechanisms as well as the structural and ideological barriers that have to date precluded such necessary reforms and perpetuated a system (and the institutions that constitute it) that continually undermines wealth gains in local communities.

Ultimately, the CRA can be regarded as a critically important tool to funnel capital back into marginalized communities. However, as the CRA has grown increasingly necessary, at the same time so has the need to reform the CRA to better regulate the modern banking industry and to motivate investment in community wealth building approaches that are gaining traction but have largely been overlooked by traditional banks. Moreover, the need is growing to consider the CRA as one tool in the “next system” of community investment and to look beyond the CRA for legislative solutions and other institutions to facilitate the creation of a new system, a new norm of political economic relationships and activity. The policy proposals considered and put forward in the final sections thus attempt to weigh the efficacy of various reforms and the extent to which effective reform is possible under the CRA in the modern context. This analysis demonstrates the need for a broader law that builds on the intent and mechanisms of the CRA, incremental reforms to make the CRA more effective for communities in the interim, and alternative financial institutions altogether.

The policy reform proposals further point to the need for community organizers to put pressure on policymakers and lay the groundwork for investment. Thus, a “CRA and Community Wealth building Guide” for community developers is provided alongside this working paper that summarizes many of its main points and outlines practical applications. It seeks to provide immediate practical guidance on where to find CRA resources and how the CRA can be used as a tool in financing and facilitating community wealth building efforts in local communities.



# Part 1: A resilient 40 years

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## A modest law of major consequence

The goal of the Community Reinvestment Act (CRA) when it was originally passed was simple: to get banks to lend in the communities where they have deposit-taking branches. The original legislation, running just a few pages long as part of the 1977 housing bill, states simply that “regulated financial institutions” are required to meet “the credit needs of [their] entire community, including low- and moderate-income neighborhoods,” and further that they “have a *continuing and affirmative obligation* to help meet the credit needs of the local communities in which they are chartered... consistent with the safe and sound operation of such institutions” (emphasis added).<sup>3</sup> The regulatory agencies to which the CRA delegated authority for the Act’s full implementation subsequently proposed and implemented regulations specifying that such provision of credit take the form of loans, investments, and services primarily geared towards homeownership, small business, and economic development purposes in low- and moderate-income (LMI) communities.<sup>4</sup>

3 U.S. Congress. “Community Reinvestment Act of 1977”. Title VIII of the Housing and Community Development Act of 1977. <https://www.fdic.gov/regulations/laws/rules/6000-1500.html>.

4 The agencies, according to the original act, include the Office of the Comptroller of the Currency, the Federal Deposit Insurance Corporation, and the Board of Governors of the Federal Reserve System (to which the Office of Thrift Supervision was later added but then removed again in 2010). LMI communities are those with less than

Such a law may at first seem unnecessary, given that banks in their modern incarnation were set up to take deposits from the public and, in turn, provide a greater quantity of money than was previously available to a given individual or business in the form of a loan or investment. However, if nowhere else than its title, the Act points to a failure of the market (specifically, banks), in that wealth taken from certain communities fails to be *reinvested* into those communities. More specifically, at the time the CRA was passed, deposits were being taken from poorer, non-white areas of communities and being invested outside these areas, in a practice often known as “redlining.”<sup>5</sup>

Though the CRA itself does not make specific reference to redlining or race, issues of racial discrimination in finance were top of mind at the time and community organizing around redlining was in part what helped bring low-income and community investment issues to the table.<sup>6</sup> The Act passed shortly after a slew of legislation that directly addressed the issue

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80 percent of the median income within a relevant assessment area.

5 Redlining gets its name from the maps drawn by banks and others to designate where (whiter and more affluent areas) and where not (black and Hispanic communities) to provide services. See: Berry, Michael V. “Historical Perspectives on the Community Reinvestment Act of 1977”. *Federal Reserve Bank of Chicago: ProfitWise News and Views*. December 2013; Keane Batt and Steve Dubb. “Educate and Empower: Tools for Building Community Wealth.” The Democracy Collaborative. August 2015.

6 Berry, Michael V. “Historical Perspectives on the Community Reinvestment Act of 1977”. *Federal Reserve Bank of Chicago: ProfitWise News and Views*. December 2013.

of discriminatory credit practices leading to racial wealth divisions within communities—namely the Fair Housing Act of 1968, the Home Mortgage Disclosure Act (HMDA) of 1975, and the Equal Credit Opportunity Act of 1976. Among this series of regulations, the CRA stands out as an acknowledgement that simply prohibiting discriminatory lending does not sufficiently address inequities in financial opportunity. That is, it sought to encourage banks to actively engage with the entirety of their communities, including low-income areas and communities of color, rather than to passively “not discriminate” against particular applications for credit.

**The CRA stands out as an acknowledgement that simply prohibiting discriminatory lending does not sufficiently address inequities in financial opportunity.**

At the time the act was passed, banks only operated branches in the states in which they were chartered and were prevented by law from branching across state lines. So, the “communities in which [banks] are chartered” were the communities surrounding where a bank had a deposit-taking branch, making bank branches the mechanism for activating CRA requirements (for all deposit-taking banks other than credit unions). To carry out this objective, the CRA utilizes the notion that the purpose of a *public* bank charter is to serve the needs of the public in the area in which the bank is chartered.<sup>7</sup> A failure to serve those needs per the terms of the CRA is to be taken into consideration in a banks’ application for mergers or other applications with regards to its charter status.<sup>8</sup>

7 Getter, Darryl. “The Effectiveness of the Community Reinvestment Act.” Congressional Research Service Report for Congress. January 7, 2015.

8 Specifically, the original legislative language states that regulators will take into account a bank’s record of meeting the credit needs

This notion that a bank’s public charter obligates it to provide a public service (beyond its strictly economic functions of lending and investing) is a relatively straightforward but consequential concept at the core of the CRA. It not only had the effect of turning banks’ attentions to the capital needs of the communities banks operate in, but took a step toward redefining the historically constructed notional distinction between ‘market’ and ‘government’ functions by requiring banks to address the social and economic issues facing communities rather than requiring the government to simply step up spending and social programs (a redefinition and legal argument that may be critical to further reform, as discussed in Part 3). This notion was not entirely new at the time. It echoed an assertion by the Federal Reserve in a 1972 clarification of bank holding company law, which stated that “bank holding companies<sup>9</sup> possess a unique combination of financial and managerial resources making them particularly suited for a meaningful and substantial role in remedying our social ills.”<sup>10</sup>

The focus on banks as opposed to public spending to address the issue of community investment was a strategic choice by organizers behind the legislation, as Ron Grzywinski—cofounder of the nation’s first community development bank, one of the original CRA organizers and only banker to testify in favor of the CRA—shares.<sup>11</sup> He recalls that the impetus to target banks specifically emerged as community developers at the time were seeing the Nixon and Ford administrations repeal Johnson administration-era legislation designed to provide federal support for community building efforts. The CRA ultimately

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of its entire community in its evaluation of a bank’s application for a “deposit facility.” An application for a deposit facility includes: a national bank charter, deposit insurance in connection with a newly chartered bank, establishing a domestic deposit-taking branch, merging or consolidating with a regulated financial institution, or acquiring shares of a regulated financial institution (“Community Reinvestment Act of 1977”).

9 Bank holding companies are companies that own banks and other nonbank companies that provide financial services.

10 “§ 225.127 Investment in corporations or projects designed primarily to promote community welfare.” *Code of Federal Records*. January 1, 2017 edition. <https://www.gpo.gov/fdsys/pkg/CFR-2017-title12-vol3/pdf/CFR-2017-title12-vol3-sec225-127.pdf>

11 Interview with Ron Grzywinski.

came as a result of a 1976 convening of community organizers and developers across the country to discuss the best way to deal with the coupled issues of redlining and community development, and the simple language of the Act utilizing the public charter argument allowed it to be tacked onto the housing bill the following year (see “The origins of the Community Reinvestment Act” later in this chapter).<sup>12</sup>

In introducing the bill, the act’s author and sponsor, Senator William Proxmire (D-Wisc.), said, “A public [banking] charter conveys numerous economic benefits [for bankers] and in return it is legitimate for public policy and regulatory practice to require some public purpose.”<sup>13</sup> The economic benefits called out by Proxmire included both the banks’ profits garnered from the legal permission given by the government to perform their lending and investing activities (in the form of a bank charter) as well as the federally funded deposit insurance available to the banks in the event of a crisis to prevent a bank run.

Arguably, the economic benefits for banks, and any private market institution, go quite beyond this given that the government puts in place a regulatory framework to support market functioning in the first place. Yet, at the time, the CRA was primarily concerned with “releasing all the nation’s bank’s energy” on the issues of redlining and community investment and “to get them to utilize their unique power and resources to work in communities nationally”—as opposed to attempting to put forward a complete redefinition of the relationship between the market and government—notes Grzywinski.<sup>14</sup> Thus, the Act’s supporters and architects used the most convenient legal tools available to them at the time—that of public bank charters. Moreover, targeting deposit-taking banks and using branches (and now also ATMs) as the mechanism for CRA requirements made sense at the time given that banks were primarily in the business of taking the public’s deposits and savings and lend-

ing that money out (and a majority of the public’s savings were held with deposit-taking banks, as opposed to being invested in the stock market).

Using this simple but powerful notion and regulatory language, the CRA can be credited in part with successfully pushing banks to overcome the initial hurdle of providing any greater amount of lending in LMI communities, including, to some extent, communities of color. As former Chairman of the Federal Reserve, Ben Bernanke notes, “it appears that, at least in some instances, the CRA has served as a catalyst, inducing banks to enter underserved markets that they might otherwise have ignored. At its most successful, the CRA may have had a multiplier effect, supplementing its direct impact by stimulating new market-based, profit-driven economic activity in lower-income neighborhoods.”<sup>15</sup> So, whereas before banks were not lending in certain communities due to racial discrimination and perceived risk or unprofitability, these communities have now become more central to banking activities. As a result, Mark Pinsky writes, “the fringe markets of the 1970s and 1980s are rapidly becoming the broadcloth of the U.S. and global economy and will continue for decades to come.”<sup>16</sup>

Moreover, in the 40 years since the CRA was first enacted, the law has been responsible for channeling hundreds of billions of dollars into LMI communities, and leveraging trillions more given that CRA dollars can come in the form of grants or participations on loans and investments as part of much larger financing packages. CRA lending data shows that between 1996 and 2014, over \$900 billion went to small business loans in low and moderate-income communities, and nearly \$800 billion went towards community development loans supporting affordable housing and economic development projects in LMI communities.<sup>17</sup> Using data on mortgage lend-

12 Ibid.

13 Quoted in Berry, Michael. “Historical Perspectives on the Community Reinvestment Act of 1977.” *Profit Wise News and Views: Federal Reserve Bank of Chicago*. December 2013: 1-6.

14 Interview with Ron Grzywinski.

15 Bernanke, Ben. “The Community Reinvestment Act: Its Evolution and New Challenges.” Speech at the Community Affairs Research Conference, Washington, D.C. March 30, 2007.

16 Pinsky, Mark. “CRA 2.0: Communities 2.0.” *Revisiting the CRA: Perspectives on the Future of the Community Reinvestment Act*, Federal Reserve Banks of Boston and San Francisco. February 2009.

17 Silver, Josh. “The Community Reinvestment Act: Vital for Neighborhoods, the Country and the Economy.” *National Community*

ing to LMI borrowers available through the Housing Mortgage Disclosure Act, a Treasury Department study found that “CRA-covered lenders increased their home mortgage loans to low- and moderate-income areas and borrowers by 39 percent from 1993 to 1998, more than twice the increase (of 17 percent) to middle and upper-income borrowers and areas.”<sup>18</sup> A 2017 study by the Federal Reserve Bank of Philadelphia further found that an LMI area that loses CRA coverage can experience between a 10 and 20 percent loss in mortgage lending.<sup>19</sup> Similarly, a 2017 study of small business lending patterns suggests that at least for the years from 1996 to 2002 and from 2012 to 2014, banks responded to CRA incentives to lend to moderate-income, small-business borrowers.<sup>20</sup>

The CRA has also helped kickstart community development efforts, with a network of community development corporations (CDCs), community development financial institutions (CDFIs), and other community development institutions growing out of CRA financing. For CDFIs—financial institutions certified to serve low- and moderate-income communities—CRA-motivated capital has become a primary source of funding since their initial establishment in 1994; in 2013 banks provided \$1.7 billion to CDFIs while the government provided about \$290 million (about five times less).<sup>21</sup> CDCs, which work on the ground in local communities to identify and work towards community development goals, receive financing that falls under the category of community development lending. Bernie Mazyck, Director of the South Carolina Association for Community Economic Development (SCACE), comments that “the CRA played a significant part” in getting banks involved with community

development efforts via community development organizations and, consequently, the growth of the network of CDCs throughout the Carolinas beginning in the 1980s and ’90s.<sup>22</sup>

The successes of the CRA are significant, particularly in comparison to the simplicity of the aims and language of the law as it was first enacted, and certainly in comparison to the absence of credit provision that may have occurred had the CRA never been enacted. Moreover, the deposit-taking function of banks—and thus the coverage of the CRA—remains immense today; as of June 2018, commercial banks held nearly \$12.1 trillion in deposits.<sup>23</sup> For this reason, the CRA should not be discounted; it has proven itself to be an important historical piece of legislation and remains a key pillar of the financial regulatory framework today. If nothing else, it was and remains an important organizing tool to provide a concrete framework for communities to organize around, whereas before re-investment demands were more amorphous.<sup>24</sup>

However, three observations are equally pertinent to make regarding CRA implementation:

**1. CRA-motivated, community-based lending and investing remains relatively small when compared to the overall deposit capacity of the banks.** The dollar volume of loans to small businesses over a nearly 20-year period, \$900 billion, amounted to just under 8 percent of the deposit capacity of banks for the single year of 2016, with a similar breakdown for CRA community development loans.<sup>25</sup> This can certainly be attributed to the fact that average loan amounts for small business by definition remain relatively small. However, comparing this lending with commercial bank

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*Reinvestment Coalition*. June 2016.

18 Taylor, John. “CRA’s Anniversary: Much to Celebrate and Much Yet to Do.” *Affordable Housing Finance*. November 1, 2007.

19 Ding, Li and Nakamura, Leonard. “Don’t Know What You Got Till It’s Gone – The Effects of the Community Reinvestment Act (CRA) on Mortgage Lending in the Philadelphia Market.” *Federal Reserve Bank of Philadelphia*. June 19, 2017.

20 Bostic, Raphael and Lee, Hyojung. “Small Business Lending Under the Community Reinvestment Act.” *Cityscape: A Journal of Policy Development and Research*. Vol 19(2). 2017.

21 “20 Years of Opportunity Finance—1994-2013: An Analysis of Trends and Growth.” *Opportunity Finance Network*, November 10, 2015: 11

22 Interview with Bernie Mazyck.

23 “Deposits, All Commercial Banks.” *Federal Reserve Bank of St. Louis Economic Data*. 2017. <https://fred.stlouisfed.org/series/DPSACB-W027SBOG>

24 Email correspondence with Bob Kuttner.

25 Calculated based on \$900 billion as the dollar volume of loans to small businesses (see: Silver, Josh. “The Community Reinvestment Act: Vital for Neighborhoods, the Country and the Economy.” *National Community Reinvestment Coalition*. June 2016) and deposit capacity of \$11.5 trillion (see: “Deposits, All Commercial Banks.” *Federal Reserve Bank of St. Louis Economic Data*. 2017. <https://fred.stlouisfed.org/series/DPSACBW027SBOG>)

investments in mortgage-backed securities—which was around 15 percent of deposits for the single year of 2016—in part demonstrates the degree to which bank activity is not centered in LMI or community development lending or investing.<sup>26</sup>

**2. As the CRA was coming to fruition, massive shifts in the economy and banking industry were already underway to move banking away from a focus on deposit-taking branches.** As a result, there has been a drop in bank deposits: In 1977 almost 70 percent of Americans’ long-term savings were in bank deposits; in 2017 that number was around 10 percent.<sup>27</sup>

**3. The 2007-2008 financial crisis resulted in more than \$19 trillion dollars in household wealth losses between 2007 to 2009.**<sup>28</sup> These wealth setbacks were felt the most in communities of color, as Black families experienced declines in wealth in the years following the crisis while median White households experienced no loss. Black families were left with “unequal opportunity to rebuild wealth coming out of the crisis, leading to widening racial disparities.”<sup>29</sup> These disparities grew despite the continued implementation of the CRA.

The intent of making these observations here is not to say that the CRA has become irrelevant. Rather, the observations point to the need for reform to compel *even more* involvement from banks and provide evidence that banks could be using more of their current deposit-taking capacity towards CRA purposes. Indeed, there are opportunities to strengthen the applicability of the CRA to banks within the modern banking context and extend it to non-banks. Lastly,

26 “Treasury and Agency Securities: Mortgage-Backed Securities (MBS), All Commercial Banks.” Federal Reserve Economic Data, Federal Reserve Bank of St. Louis. Updated May 29, 2017. <https://fred.stlouisfed.org/series/TMBACBW027SBOG>

27 Pinsky, Mark. “CRA 2.0: Communities 2.0.” Revisiting the CRA: Perspectives on the Future of the Community Reinvestment Act, Federal Reserve Banks of Boston and San Francisco. February 2009. “Americans Still Favor Real Estate for Long-Term Investment.” Gallup. April. 21, 2017. <http://www.gallup.com/poll/208820/americans-favor-real-estate-long-term-investment.aspx>

28 *The Financial Crisis Response in Charts*. The Department of the Treasury. April 2012. [https://www.treasury.gov/resource-center/data-chart-center/Documents/20120413\\_FinancialCrisisResponse.pdf](https://www.treasury.gov/resource-center/data-chart-center/Documents/20120413_FinancialCrisisResponse.pdf)

29 Burd-Sharps, Sarah and Rasch, Rebecca. “Impact of the US Housing Crisis on the Racial Wealth Gap Across Generations.” Social Science Research Council. June 2015.

they point to the need to consider the CRA as part of a broader framework of banking legislation and institutions, one of multiple interventions to protect wealth gains and promote economic stability in an atmosphere of discriminatory credit practices and recurrent economic crisis. Indeed, Grzywinski says, “[the CRA] codified that banks have this special obligation to invest in community development. That is the language of the law[...]. In my opinion, banks are not obeying the letter or spirit of that law.”<sup>30</sup> This

## **There are opportunities to strengthen the applicability of the CRA to banks within the modern banking context and extend it to non-banks.**

observation further begs the question of why such reforms have not been implemented over the course of the last 40 years.

## **Evolution of the CRA: Resilience and stagnation**

The Community Reinvestment Act originally set out to address a failure of the market, specifically the failure of banks to equitably provide financial opportunities in the communities where they operated, by utilizing the mechanism of the public charter of depository institutions (i.e. banks that take deposits) and the publicly funded deposit insurance afforded through it. However, at the same time the CRA was being developed, shifts in the banking industry were already underway that deemphasized the role of traditional depository institutions and bank branches—the mechanism at the heart of the CRA to activate CRA obligations. Services provided by investment banks and brokerage firms, in part motivated by market pressures of the time, grew in prominence and began to redefine the course of the banking indus-

30 Interview with Ron Grzywinski.

try and bank policy. A critical turning point came in 1976 with the advent of money market mutual funds and cash management accounts created by brokerage firms. These cash management accounts offered basically the same savings and deposit services of commercial banks, but with a higher rate of return for depositors, essentially allowing non-depository institutions to compete with commercial (and at that time, strictly depository) banks.<sup>31</sup>

The funds collected through money market accounts would gravely challenge the separation of commercial and investment banking activities established in the Glass-Steagall Act of 1933. Economists have since pointed to this lack of separation as a driver of financial volatility and crises due to the adverse incentives created by allowing the same institution to both take deposits and engage in investment banking activity such as security trading. The cash management accounts specifically undermined the function of Regulation Q (of Glass-Steagall), which had established a limit on deposit rates to prevent competition between investment and commercial banks.<sup>32</sup> Instead, commercial banks were forced to compete, which was difficult due to a combination of broader market pressure and regulations that prevented commercial banks from performing financial activities outside of straightforward deposit-taking and lending or adjusting interest rates on deposits and loans. As public savings moved out of commercial banks and into cash management accounts, commercial banks faced tighter profit margins.<sup>33</sup>

Thus, the brokerage firms' advent of cash management accounts sparked a fundamental shift in the banking industry, and regulators were forced to respond as competitive pressures grew between commercial and investment banks. As Mark Pinsky, CDFI industry leader and President and CEO of Five/Four Advi-

sors reflects, "in July 1977, [investment bank] Merrill Lynch entered the market with a cash management account. All banking law since then is entirely just to deal with that one event. It broke the banking system, because then you didn't need a [federally insured depository] bank to do banking anymore."<sup>34</sup>

Legislation throughout the late 1980s gradually allowed commercial banks more freedom in the types of lending and investing they engaged in (such as offering adjustable-rate mortgages, investing in junk bonds, and securitizing mortgages). The passing of the Riegle-Neal Act in 1994 allowed for interstate banking, meaning banks could open branches across state lines (which would require CRA review if done either via opening a new branch or merging).<sup>35</sup> The 1999 Gramm-Leach-Bliley Act allowed for securities firms and insurance companies to buy banks and for commercial banks to finance insurance and real estate activities.<sup>36</sup> In the end, where banks were previously only allowed to open branches within a particular state, and where commercial bank activities (i.e. lending and depositing) were separated from investment bank activities (i.e. security trading), these final pieces of legislation allowed full integration of banking activities, signifying the full repeal of Glass-Steagall-era legislation. Not to mention, technological advances over this time period facilitated the volume and complexity of financial activity and allowed a greater share of financial activity to occur remotely (without bank branches) and via online, non-bank companies (i.e. fintech).

The initial action by Merrill Lynch and the subsequent regulatory reforms was indicative of broader political economic transformations happening at the time, both domestically and internationally, as a result of ideological and structural shifts in the economy. Keynesian economic theory, which suggested state spending and intervention would support growth, gave way in the 1970s to the resurgence of free-market

31 Frederic Mishkin, *The Economics of Money, Banking, and Financial Markets: The Business School Edition (3rd Edition)*, (2012), 296.

32 Macey, Jonathan, "Reducing Systemic Risk: The Role of Money Market Mutual Funds as Substitutes for Federally Insured Deposit Banks." *Yale Law School Faculty Scholarship Series*. March 1, 2011.

33 C. Murdock, "The Big Banks: Background, Deregulation, Financial Innovation, and 'Too Big To Fail,'" *Denver University Law Review*, 90.2, 2013, p. 516.

34 Interview with Mark Pinsky.

35 F. Mishkin, *The Economics of Money, Banking, and Financial Markets: The Business School Edition (3rd Edition)*, 297.

36 Ibid.

# The origins of the Community Reinvestment Act

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By 1977, Ron Grzywinski had already marked his legacy by helping co-found the country's first community development bank, South Shore Bank, in 1973 (later renamed Shorebank). The bank emerged directly out of the civil rights organizing being done in the South Side of Chicago, and was set up, in part, as an experiment in banking law.

"In 1972, the [Federal Reserve Board of Governors] issued regulations that stated that bank holding companies could only invest in and own and control businesses closely related to the business of banking," Grzywinski explained in an interview. One of those was community development corporations, if they primarily served low-and moderate-income communities. "So it was that regulation that we used to create Shorebank, because we said to ourselves, 'if the Fed was going to allow a bank holding company to invest in a community development corporation, it would logically be possible for a bank holding company to be a community development corporation.'"

Regulators told the founders they would have to actually do it to find out if their idea was possible, since there was no precedent for such an arrangement being approved by the Federal Reserve Board of Governors. "So we created a BHC that would not only own a bank, but also a social purpose non-profit, a real estate development company, and an investment fund to support well-managed community business that could not qualify for bank credit," Grzywinski said. "That was how we intended to provide all or many of the financial and management tools a community needs to improve itself."

It was this work that got Grzywinski invited to a convening in the fall of 1976 called together by Sam Brown, who at the time was Colorado state trea-

surer and had been an anti-Vietnam war organizer. It was attended by many liberal and political activists who were concerned that many of the economic development initiatives spawned by the civil rights movement under President Johnson were being cut back under the Nixon and Ford administrations.

"They all talked about different ways a national development bank might be started," Grzywinski recalled. "The one time I spoke up, I said to the group that I thought that a national development government bureaucracy would be one narrow-necked funnel that everything would have to pass through, like the department of Housing and Urban Development. So I said, 'Why not figure out a way to release all the nation's banks' energy on this issue?' The group wasn't interested in hearing that. They didn't think that the banks would do anything, and they didn't know how the banks operated."

After the meeting, Grzywinski was pulled aside briefly by Robert Kuttner, the current co-editor of *The American Prospect* and professor at Brandeis University's Heller School who was then chief investigator on the staff of Wisconsin Senator Willism Proxmire, a prominent Democrat on banking issues. A year later, after Jimmy Carter won the presidential election, Grzywinski got a phone call: It was Kuttner, asking if he would testify in favor of a certain Community Reinvestment Act.

"I said, what is the Community Reinvestment Act?" Grzywinski recalled. "He explained it, and I said 'sure.'"

He participated in a three-day series of hearings, which included testimony from Ralph Nader, representatives from National People's Action, the president of the National Urban Coalition, and the assistant secretary for community development of HUD.

Afterward, Proxmire—who was experienced in the rules of the Senate—managed to attach very simple language to a housing bill authorizing the Community Reinvestment Act. “It was constitutional-type language because it just says ‘regulated depositories [i.e. commercial banks] have an obligation to meet the credit needs of their communities, period,’” Grzywinski said. The language was approved in a House-Senate conference committee and soon became the law of the land.

But what about that year between the convening and the call from Kuttner to testify? Kuttner explained in an interview that the idea for the CRA had its roots in years-long community organizing, particularly to investigate banks’ mortgage lending records to better understand discrepancies in bank lending. At the center of these network-building efforts for the Home Mortgage Disclosure Act (HMDA), which in turn became the momentum for the CRA, were Geno Baroni, head of National Center for Urban Ethnic Affairs, and Gale Cincotta, head of National People’s Action.

“[The HMDA organizers] looked up mortgage records and recorders and deeds, which at the time was really painstaking and hard to do. And so they said ‘if only this was public record, we could do research on who are the good guys and bad guys,’” Kuttner said.

The organizers of the HMDA had already been in touch with Proxmire in 1974, so when Kuttner joined Proxmire’s team in 1975, “the first file that was handed to me was called Mortgage Disclosure. It was about 20 groups saying, ‘what we want from Proxmire is a bill that requires disclosure of where the banks are putting loans.’”

When the Home Mortgage Disclosure Act passed in late 1975, Kuttner recalled, “then we said, ‘Hey, this is really cool—what more can we do?’” So he discussed with community groups, Grzywinski and other progressive bankers legislation “modeled on

gender and racial affirmative action to require bank activities to reflect how they’re responding to those issues.”

Kuttner said they also had in mind that “state and federal legislation going back to the 19th century speaks of ‘public convenience and necessity’ in the granting of charters to private corporations that do business with the public, and conditions the granting of such charters, or permissions to do business, on performance criteria.” Such legislation, first enacted around 1870 and up through 1920, pertained primarily to public service industries such as transportation, communications, power, and sanitary services. The organizers considered how this could be applied to the banking industry.

The decision to move the CRA through Congress instead of other options (such as the proposed national development bank) had more to do with the political climate and legislative feasibility, Kuttner said. “We had a fair majority of maybe one or two Democratic senators to get a piece of regulation like CRA through Congress. A [development] bank would raise the issue of how was it going to be financed, does it need appropriations, whereas disclosure or affirmative action was a little more trendy and [we] could get moderates to support it.”

Both Grzywinski and Kuttner point to the importance of community groups in the successful implementation of the CRA. In D.C., the Center for Community Change played a critical role, and Grzywinski specifically notes the role played by National People’s Action and the National Training and Information Center at the center of efforts in Chicago and nationally to push banks to lend more equitably in the communities that supplied deposits but received little reinvestment.

“They were very shrewd and very good organizers. They had a long view of what they were doing,” Grzywinski said.



thinking through neoclassical thought as the steady post-war growth perplexingly slowed to economic stagnation amidst larger macroeconomic transitions. These included economies shifting off the gold standard, exchange rates stabilizing, cheap oil from the Middle East being interrupted, and countries around the world recovering from their decimation during World War II and competing again with the United States' industrial strength.

Under the ensuing market pressures of 1970s stagnation, neoclassical advocates criticized Keynesian economics for this slowed growth, and market institutions began innovating and seeking out sources of inefficiencies that were perceived to be preventing growth and investment returns. Further, an orientation towards shareholder value maximization and profit as a first priority began to take hold as the “welfare capitalism” of the 1960s and 1970s gave way to financialization of the economy and as federal policy shifted toward free market-oriented neoliberal orthodoxy throughout the 1980s (elaborated further in Part 2).<sup>37</sup> To the extent that these structural and ideological shifts in the broader political economy translated into deregulatory legislation and consolidation in the banking industry, market-based intermediation grew to be the primary function of banks as opposed to straightforward deposit-taking and lending.

Given these ideological, structural and deregulatory legislative changes, it is perhaps remarkable that the CRA is still standing today. Its resilience over the last 40 years can in part be attributed to the fact that the simplicity of the language of the Act that allowed it to pass through Congress also provided no concrete criteria by which to assess banks' performance. Rather, it delegated the authority to establish the implementation framework to several federal agencies—including the Federal Reserve Board of Governors, Comptroller of the Currency, Federal Deposit Insurance Corporation, and (no longer) Office of Thrift and Supervision. This allowed flexibility in interpreting what ex-

actly the Act would entail, likely saving it from initial backlash. It also spread the institutionalization of the Act across several agencies, inhibiting reversal over the long term.

However, it also meant that the Act did not do much at the outset. Grzywinski comments that “for the first 10 years, the enforcement by regulators was weak. It was virtually ignored so that during a bank examination, if a bank gave [regulators] a one-page memo and said ‘this is our CRA policy’ it was enough [to satisfy their CRA requirements].”<sup>38</sup> The turning point for the CRA's implementation trajectory came in 1984 when Continental Illinois Bank of Chicago ran into trouble as a result of purchasing bad loans that had been originated by a bank in Oklahoma. The bank had purchased the loans in an effort to “grow more rapidly than normal—which is often disastrous for banks,” says Grzywinski.<sup>39</sup> After being taken over by the FDIC, Continental's application for an expansion was denied by the Federal Reserve Board of Governors as a result of community members' concerns about its responsiveness to community credit needs. This action by the Fed “opened everyone's eyes that going forward the CRA was serious, and that it was going to be seriously enforced,” Grzywinski says.<sup>40</sup> The move also demonstrated the true powerful potential of the Act's intent. Grzywinski comments that:

One of the wonderful requirements under [the CRA regulations] is that banks have to get permission to take certain actions, such as various kinds of expansion. Another part of the regulations is that it gives the public standing to formally be heard when the regulatory agencies review a bank's application to expand under the CRA, so that it's not a private event between regulators and the banks. It is a more transparent process in which the community has regulatory standing.<sup>41</sup>

Following this initial success, implementation and

37 Ho, Karen. “Wall Street Historiographies and the Shareholder Value Revolution”, Chapter 3 in *Liquidated: An Ethnography of Wall Street* (Duke University Press, 2009), 122-168.

38 Interview with Ron Grzywinski.

39 Ibid.

40 Ibid.

41 Ibid.

enforcement slowly moved forward. It was not until 1989—after Congress held hearings on the regulatory agencies’ enforcement of the CRA and realized they had largely been ignoring it<sup>42</sup>—that the CRA exams were introduced, and public disclosure of CRA exams was required.<sup>43</sup> In this revision, the four-tier rating system was introduced. Only two revisions followed, one in 1995 and again in 2005. The 1995 revision introduced different exams for banks of different asset sizes and changed the exam components, the most strenuous of which are exams of large banks that consist of a lending, investment, and service test (the score for which uses a numeric 24-point scale). The 2005 revision added another exam category—a “community development test”—to be conducted alongside a lending exam for “intermediate-small banks.”

## **Deregulation and changes in the structure of the banking industry helped set the stage for the 2008 financial crisis that stripped wealth from the very communities the CRA is intended to serve.**

This slow and modest implementation is partly what allowed the CRA to remain resilient in the face of structural and ideological changes occurring in the banking industry and broader political economic environment. On the other hand, the upshot for the CRA of these changes is that at the same time banks were increasingly establishing CRA offices to respond to criteria and requirement changes, the culture and function of banks were more and more moving much beyond the scope and intent of the CRA as it was initially written. As former Fed chair Ben Bernanke notes, “for some institutions, the concept of the ‘lo-

<sup>42</sup> Ibid.

<sup>43</sup> Bernanke, Ben S. “The Community Reinvestment Act: Its Evolution and New Challenges.” Speech at the Community Affairs Research Conference, Washington D.C. March 30, 2007.

cal community’ is no longer as clear as it was when the CRA was enacted; today, some institutions are not identified with a particular community but are regional or national in scope.”<sup>44</sup>

Increasingly, banking activity is happening outside of entities covered by the CRA, limiting its scope. Financial services such as deposits, savings, investments, and even lending are now being provided by such institutions as mortgage companies and online banks. In some instances, these non-CRA-covered institutions are owned by the same bank holding company as a CRA-covered bank and are performing activity outside of the CRA-covered arm in a form of regulatory arbitrage.<sup>45</sup> Moreover, mobile and online platforms have allowed greater amounts of banking activity to occur outside of deposit-taking branches and ATMs, the main mechanisms for activating CRA requirements.<sup>46</sup> Relatedly, more non-bank online financial companies (i.e. fintech companies) have emerged. While credit card companies and online banks are covered by the CRA, non-bank and non-affiliate mortgage companies as well as any non-depository investment banks, mutual funds, or hedge funds are not. Credit unions are also not covered, given their nonprofit status and inherent orientation towards their deposit base (who are members). However, credit unions do not always serve segments of the population that have traditionally faced marginalization in financing.<sup>47</sup>

Deregulation and changes in the structure of the banking industry helped set the stage for the 2008 financial crisis that stripped wealth from the very communities the CRA is intended to serve. The growth and consolidation of banks has also only further entrenched the market primacy focus of banks. Indeed, any business school graduate of the last 20 years will

<sup>44</sup> Ibid.

<sup>45</sup> Ibid.

<sup>46</sup> Seidman, Ellen. “A More Modern CRA for Consumers,” in *Revisiting the CRA: Perspectives on the Future of the Community Reinvestment Act*, Federal Reserve Banks of Boston and San Francisco. February 2009.

<sup>47</sup> Silver, Josh. “The Community Reinvestment Act: Vital for Neighborhoods, the Country and the Economy.” National Community Reinvestment Coalition. June 2016.

tell you that the primary purpose of the firm (including banks), is to maximize shareholder value, a lesson taught on day one of any introductory management or finance course. That is, despite the critical gains of the CRA in diverting a portion of the attention and resources of banks to invest in local communities, major banks remain primarily fixated on not just maintaining but maximizing their bottom line, which takes primacy over serving community needs.

Economics professor at NYU's Stern School of Business Lawrence White's reading of the CRA further illustrates this viewpoint. "If loans are profitable, profit-seeking banks should already be making them," he writes. "In this case, the CRA is redundant at best."<sup>48</sup> This criticism highlights the profit primacy orientation but ultimately misses the point. The very purpose of the Act was to serve communities previously *perceived* as unbankable by encouraging the industry to lend equitably to communities where they would not naturally extend themselves. Indeed, the CRA was successful in encouraging banks to make loans and investments or even grants vital to community development projects.<sup>49</sup>

Still, though banks now allocate significant and important capital to community groups such as CDCs and CDFIs through loans, investments, and grants, some consider this as a way of offloading their CRA responsibility. Grzywinski comments that "the bank holding companies have a unique combination of managerial resources to deal with the nation's social ills and instead of making only gifts or grants that can be expensed, or making loans to the best CDFIs at—in my opinion—fairly high rates with low risk, they themselves could be more directly involved."<sup>50</sup> He further notes how this allows banks to remain culturally separate from community-oriented activity, further divorcing the well-paid bankers from local communi-

ties and residents.<sup>51</sup> In that sense, community groups over the last 40 years have to some extent taken on the work of community investment and development the Act's original thinkers intended the banks to become more involved in.

Meanwhile, these same structural, ideological, and legislative changes that constrained the CRA's impact also prevented reforms that would extend CRA requirements to the growing financial activity outside of branches and depository institutions or increase the rigor of bank examinations and CRA requirements. As the banking industry grew, so too did the bank lobby to become the largest lobbying presence on Capitol Hill. The revolving door between government, corporate America, and Wall Street has further institutionalized the neoliberal (deregulatory) policies that align government action with market interests.<sup>52</sup> Similarly, the now-normalized rhetoric and ideology of "the free market" as separate from "the government" provides the grounds on which to attack economic policies that suggest market institutions serve a purpose beyond profit maximization. Even if significant economic reforms were permitted to be brought to the table, some research also points to the role of polarization in Congress and the electorate in impeding bipartisan cooperation and the passage of legislation.<sup>53</sup>

This political climate has meant a reluctance to call too much attention to the CRA in recent decades, due to a fear that putting forward major reforms might lead to complete repeal by Congress. According to Josh Silver, Senior Advisor at the National Community Reinvestment Coalition (NCRC), "in my 20-year career, there's been two or three times where there were

48 White, Lawrence. "The Community Reinvestment Act: Good Goals, Flawed Concept." Chapter in *Revisiting the CRA: Perspectives on the future of the Community Reinvestment Act*. Federal Reserve Banks of Boston and San Francisco. February 2009.

49 Zinman, Jonathan. "The Efficacy and Efficiency of Credit Market Interventions: Evidence from the Community Reinvestment Act." Joint Center for Housing Studies, Harvard University. July 2002.

50 Interview with Ron Grzywinski.

51 Ibid.

52 Fang, Lee. "The reverse revolving door: how corporate insiders are rewarded upon leaving firms for Congress." *The Nation*. May 4, 2013.

53 Brady, David W. and Hahrie Han, "Our politics may be polarized. But that's nothing new," *The Washington Post*, January 16, 2014, <https://www.washingtonpost.com/news/monkey-cage/wp/2014/01/16/our-politics-may-be-polarized-but-thats-nothing-new/>. Desilver, Drew. "The polarized Congress of today has its roots in the 1970s." Pew Research Center. June 12, 2014. <http://www.pewresearch.org/fact-tank/2014/06/12/polarized-politics-in-congress-began-in-the-1970s-and-has-been-getting-worse-ever-since/>

opportunities [for a CRA modernization effort]...You need a strong social movement, you need a different temperament in Congress, and you need bipartisan consent—that is extraordinarily hard to do.”<sup>54</sup>

The last major attempt was made in 2009 with the introduction of the *Community Reinvestment Modernization Act* by Representative Eddie Bernice Johnson (D-Tex.), but it did not make it out of the House Financial Services Committee. The data disclosure improvements (namely, disclosure of loan terms and conditions as well as the race and gender of small business borrowers) called for in the bill, however, were incorporated into the 2010 Dodd-Frank Wall Street Reform and Consumer Protection Act, which is important for increasing the transparency and accountability of bank lending.<sup>55</sup> Ellen Seidman, former director of the Office of Thrift Supervision and former board member of the FDIC, says that a more recent effort to make significant changes from within the regulatory agencies was attempted in 2011 but also fell through. “Essentially regulators decided, with the likely political blowback on [Capitol] Hill, to not rock the boat,” she recalls.<sup>56</sup> (A very recent CRA modernization bill was introduced by Senator Elizabeth Warren in September 2018).<sup>57</sup>

The Dodd-Frank Act, passed as a response to the 2008 financial crisis, was in some ways an anomaly to political stagnation, if only initiated by the severity of the crisis and ensuing public backlash (as well as Democratic Party control of both houses of Congress and the presidency). Dodd-Frank (along with its international counterpart, Basel III) sought to address many of the issues at the root of the crisis, including by establishing the Consumer Protection Financial Bureau to investigate bank lending practices and by

identifying the largest, systemically relevant banks to be subject to capital requirements and submission of living wills (which outlines the institutional structure of the financial institution and states who is to be held accountable financially in the event of bank’s failure). The law further set mortgage underwriting standards, barred commercial banks from security trading (via the “Volcker Rule”), and established the Orderly Liquidation Authority (OLA) to facilitate the handling of failing banks and avoid government bailout.<sup>58</sup>

Assuming successful ongoing implementation of key Dodd-Frank provisions (which is not guaranteed given systemic attempts to weaken or undermine the law in recent years), the efforts of the CRA are at lesser risk of being undermined by economic collapse. Dodd-Frank implementation proved elusive for several years after its passing, due to the same political barriers that work against reformative economic policy. Only in 2017—with Wells Fargo finally passing its living will review (its third attempt) and all financial institutions passing their stress tests, demonstrating that they had accumulated adequate and appropriate capital to withstand a bank failure and therefore do not present a threat to the financial system—did the remaining significant portions of Dodd-Frank become fully implemented.<sup>59</sup> In doing so, the banks dodged prior regulatory admonitions that, should they fail to meet their capital requirements and submit living wills, they would be subject to being split along business lines.<sup>60</sup> However, President Trump’s

54 Interview with Josh Silver.

55 Email correspondence with Josh Silver; Silver, Josh. “How Data Disclosure Will Help Prevent the Next Financial Crisis.” *Shelterforce*. February 23, 2017. <https://shelterforce.org/2017/02/23/how-data-disclosure-will-help-prevent-the-next-financial-crisis/>

56 Interview with Ellen Seidman.

57 “Warren Unveils Historic Legislation to Confront America’s Housing Crisis.” Elizabeth Warren – Press Releases. September 26, 2018. <https://www.warren.senate.gov/newsroom/press-releases/warren-unveils-historic-legislation-to-confront-americas-housing-crisis>

58 Peirce, Hester and Broughel, James. “Dodd-Frank: What It Does and Why It’s Flawed.” Mercatus Center at George Mason University. 2012. <https://www.mercatus.org/system/files/dodd-frank-FINAL.pdf>

59 Hamilton, Jesse. “Wells Fargo’s Living Will Approved After Third Try.” Bloomberg. April 24, 2017. <https://www.bloomberg.com/news/articles/2017-04-24/wells-fargo-s-third-time-a-charm-as-it-clears-living-will-hurdle>. Hoffman, L and Tracy, R. “Fed ‘Stress Tests’ Clear All Banks to Issue Payouts to Shareholders.” *The Wall Street Journal*. June 28, 2017.

60 Tracy, Ryan. “FDIC’s Hoenig Keeps Wall Street on Edge.” *The Wall Street Journal*. September 25, 2014. Though it is not in the scope of this report to weigh the merits of “breaking up the banks” as a solution to community investment issues, it is worth briefly noting that the barriers to doing so are the same (in terms of political and economic consequences), if not greater, as for CRA reform, given the costs and difficulty associated with actually separating banking activities in the era of the primacy of market-based financial intermediation (and the risk of forcing activity into the shadow markets).

administration has since issued rollbacks to the regulation, most notably by increasing the asset threshold requirement for Dodd-Frank's capital requirements and stress tests from \$50 billion to \$250 billion (limiting the applicability of such requirements from 38 to 12 banks).<sup>61</sup> Fortunately, thus far, other major reforms, such as the Consumer Financial Protection Bureau, remain statutorily intact, even though the CFPB's role has been weakened by efforts of the Trump administration to limit its enforcement powers and with the appointment of former Republican congressman Mick Mulvaney, a chief CFPB opponent, as acting director of the Bureau.<sup>62</sup>

The same structural and ideological changes that have presented a constraint to extending the CRA and enacting stricter regulatory requirements on banks are also what have prompted communities to innovate and develop new opportunities and models to build local and collective ownership—opportunities and models that can be worked into the CRA regulatory framework. As Gar Alperovitz and colleagues at TDC write, “the inability of traditional politics and policies to address fundamental challenges has fueled an extraordinary amount of experimentation in communities across the United States and around the world.”<sup>63</sup> That is, communities either exploited and pushed out by the present system or that are responding proactively to the economic insecurity and alienation of free-market primacy have turned to alternative models that seek to bypass the shortcomings of the market to provide greater shared wealth and economic security, activities and institutions such as

cooperatives, land trusts, and municipal enterprises.

The potential for making better use of the outcomes of this experimentation—namely, community wealth building approaches within the CRA as it is currently written 21<sup>st</sup> century—is the focus of Part 2.

## The CRA regulatory framework today

The CRA has remained resilient over the last 40 years despite the structural and ideological changes that have further moved political and economic interests towards market primacy and deregulatory policies in the banking industry.

The CRA regulatory framework today is composed primarily of the “definitions” and exam criteria of low- and middle-income and community development lending (including what qualifies as CRA lending, investments, and services), alongside the exams and examiners, and the enforcement mechanisms. This regulatory framework came together through the 1995 and 2005 revisions instituted by the OCC, Federal Reserve Board, and FDIC.<sup>64</sup> These agencies are coordinated by the Federal Financial Institutions Examination Council (FFIEC), or the “interagency council,” which also coordinates other regulatory bodies uninvolved in CRA implementation (such as the National Credit Union Administration and the Consumer Financial Protection Bureau).<sup>65</sup> Thus the “interagency council” does not itself have rulemaking authority, and each of the agencies named by the CRA are responsible for their own CRA regulations. (For practical and political reasons, these regulations are the same on paper across all three agencies, though their interpretations may differ.)<sup>66</sup> The OCC has regulatory and exam authority over federal chartered banks and thrifts; the Fed—which is primarily responsible for monitoring the U.S. money supply and stabilizing the national economy—covers state-chartered member banks; and the FDIC covers state-chartered nonmember banks.

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Moreover, the Dodd-Frank law, as fully implemented, arguably instills partial separation (via “the Volcker Rule”) and the provision of capital requirements and living wills do all that can be done outside of separation to hold investors more accountable to losses. Thus, this report leaves aside this issue to focus on community investment concerns assuming, at a minimum, the continuation of the Dodd-Frank-era financial structure and regulation.

61 Werner, Erica, and Merle, Renae. “Congress approves plan to roll back post-financial-crisis rules for banks.” *The Washington Post*. May 22, 2018.

62 Merle, Renae. “Trump administration strips consumer watchdog office of enforcement powers in lending discrimination cases.” *The Washington Post*. February 1, 2018.

63 Alperovitz, Gar et al. “The Next System Project: New Political-Economic Possibilities for the 21st Century.” *The Democracy Collaborative*. March 2015.

64 Originally the OTS was part of this regulatory framework, but its role was terminated with Dodd-Frank and its functions were absorbed by the OCC. Email correspondence with Ellen Seidman.

65 Email correspondence with Ellen Seidman.

66 Ibid.

# Wall Street crash: It was the system, not the CRA

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Structural, ideological, and legislative changes that diverged the banking industry's interests from those of local communities set the stage for the 2007-2008 financial crisis that stripped away the hard-won wealth gains of low-income communities.

In traditional financial intermediation, a bank takes household deposits and lends this money to borrowers (less its required reserves). What dominates in today's economy, however, is market-based financial intermediation, which involves multiple institutions that operate in the capital markets. Here, a significant portion of bank balance sheets become tied to the stock market itself, so that market-based intermediaries both operate in, and themselves significantly constitute, the financial markets.<sup>1</sup>

Systemic risk has increased as a result. A failure of one institution sets off a chain reaction, leading to a liquidity crisis. Then, due to their systemic relevance and inadequate capital reserves to cover losses, the government is forced to inject credit into the markets in order to avoid economic collapse (a problem known more colloquially as "too big to fail").

One of the most important questions regarding the financial crisis is what, in addition to structural factors, caused the banks to fail in the first place. One set of explanations points to banks offering loans with hidden costs to unqualified borrowers (what's often considered predatory lending) that were then packaged into mortgage-backed securities to be sold to other financial institutions, which repackaged them into other securities (collateralized debt obligations), rated their quality significantly higher than they should have been, and then engaged in

frenzied trading of those assets to maximize returns.<sup>2</sup> Bank managers pressured and incentivized to "maximize shareholder value," and top executives far removed from the activities occurring across the bank's functions, overlooked the underlying risk of those assets.<sup>3</sup> International factors, such as the U.S. economy's ability to attract global capital and its use of deficit spending (as opposed to taxation) to finance the Iraq and Afghanistan wars, contributed to the boom-and-bust cycles.<sup>4</sup>

As the Community Reinvestment Act successfully shifted some of the banking industry's attention to previously ignored lower-income communities, some critics have tried to argue that the CRA encouraged banks to do reckless lending. However, numerous studies carried out by the Federal Reserve and others have shown that the high-cost, risky lending to unwitting borrowers during the crisis was primarily carried out by non-banks not covered under the CRA. Only 6 percent of crisis-related lending was performed by CRA-covered lenders in CRA demographics.<sup>5</sup> Perhaps most importantly, the CRA explicitly stipulates that banks lend to low- or moderate-income communities consistent with safety and soundness concerns. So even if banks were motivated by the CRA to provide loans to unqualified borrowers, they would have been doing so in noncompliance with the language of the CRA.

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1 T. Adrian, and H. Shin. "The Changing Nature of Financial Intermediation and the Financial Crisis of 2007-09". *Federal Reserve Bank of New York Staff Reports, Staff Report No. 429*. April 2010. 3.

2 F. Mishkin, *The Economics of Money, Banking, and Financial Markets: The Business School Edition (3rd Edition)*, 201-203.

3 "Risk Taking By Banks: The Role of Governance and Executive Pay." Chapter in *The Global Financial Stability Report: Risk Taking, Liquidity, and Shadow Banking – Curbing Excess While Promoting Growth*. International Monetary Fund. October 2014), 106-107.

4 See Thomas Oatley's 2015 book, *A Political Economy of American Hegemony*.

5 Kroszner, Randall. "The Community Reinvestment Act and the Recent Mortgage Crisis." *Revisiting the CRA: Perspectives on the Future of the Community Reinvestment Act*, Federal Reserve Banks of Boston and San Francisco. February 2009. p.9.

The definition and criteria of community development that inform the CRA exams were introduced with the 1995 revision. The exams provided a more standardized way for regulatory agencies to assess banks' CRA performance and thus fulfill the statutory requirement to take that into consideration during reviews of applications for mergers and expansions (the main enforcement mechanism stipulated in the original legislation). The exams ensured that banks were to be assessed in three areas: lending, investing, and services. The 2005 revisions marginally built on this initial structure by adjusting the exam requirements for banks according to their asset size (summarized in the table on page 22); this revision resulted from the belief that CRA exams needed to be streamlined for smaller banks, though a number of community groups believed the revisions went too far in lowering the requirements for smaller banks. This revision further introduced a "community development test" for medium-sized banks—which assesses their lending, investments, and services related to community development—in lieu of the investment and services test.<sup>67</sup> Banks are assessed based on their performance in their "assessment areas," or the areas where the bank has branches or deposit-taking ATMs.

### *Definitions and examination criteria*

The primary way the CRA specifies what qualifies as community development is through a document called the "Interagency Questions & Answers." Given that the original language of the CRA was quite simple, the Q&A documents are the primary way through which the regulatory agencies expound upon what exactly "serving the credit needs of their communities" means. Additional guidance is also provided through examination procedures published by the agencies). The document is updated periodically by pulling together hundreds of comments submitted by banks, community groups, and "others." Each time it is revised, the Q&A document responds at length to these comments, specifying which were ultimately

67 "OCC Bulletin 2005-28: The Community Reinvestment Act". Office of the Comptroller of the Currency, U.S. Department of the Treasury. August 24, 2005.

incorporated into the final revisions, which were not, and why. It then provides definitions and specific examples of what loans, investments, and services do or do not qualify toward CRA compliance.

The Q&As thus provide the baseline definition and criteria for what qualifies as community development across the regulatory framework, and the banks are expected to follow the Q&As guidelines when performing and categorizing their CRA lending, investments, and services.

### *Community development criteria*

The baseline definition of "community development" put forward in the most recent Q&A (updated July 25, 2016) states that community development activities are defined as those "that promote economic development by financing businesses or farms that meet the size eligibility standards of the Small Business Administration's Development Company (SBDC) or Small Business Investment Company (SBIC) programs... or have gross annual revenues of \$1 million or less."<sup>68</sup> Some considerations are also given to other social services within this definition (such as workforce development and revitalization or stabilization activities for low- and middle-income areas).

It elaborates later in the document that community development is not strictly limited to economic concerns, stating that:

Although the definition of 'community development' includes activities that promote economic development by financing small businesses or farms, the rule does not limit community development loans and services and qualified investments to those activities. Community development also includes community or tribal-based child care, educational, health, social services, or workforce development or job training programs targeted to low-or moderate-income persons, affordable housing for

68 "Community Reinvestment Act; Interagency Questions and Answers Regarding Community Reinvestment; Guidance." *Federal Register: Rules and Regulations*. Vol. 81, No. 142. Monday, July 25, 2016.

## Bank testing under the Community Reinvestment Act

	Lending test 12 points, 50% weight	Investment test 6 points, 25% weight	Services test 6 points, 25% weight	Community development 12 points, 50% weight
<b>Small</b> < \$305 million in assets	Required	Optional	Optional	Not applicable
<b>Intermediate-small</b> \$305 million – \$1.221 billion in assets	Required	Not applicable	Not applicable	Required
<b>Large</b> > \$1.221 billion in assets	Required	Required	Required	Not applicable

low- or moderate-income individuals, and activities that revitalize or stabilize low- or moderate-income areas, designated disaster areas, or underserved or distressed nonmetropolitan middle-income geographies.<sup>69</sup>

### Lending criteria

The lending criteria are also central to the CRA, both because the lending test makes up 50 percent of all banks' overall exam rating and because the provision of financing to low- or moderate-income communities was the central aim of the CRA. The focus in the lending category is, like the community development test, on small business and small farm lending, but with the major addition of home mortgage lending and other forms of retail lending to LMI borrowers. Qualifying lending to small businesses includes loans to businesses with revenue under \$1 million or loans to small businesses in LMI tracts. Low-income borrowers are defined as earning below 50 percent of median family income in the relevant assessment area, while moderate-income borrowers are defined as earning below 80 percent of median family income.<sup>70</sup>

<sup>69</sup> Ibid.

<sup>70</sup> Horowitz, Ben. "Defining 'low-and moderate-income' and 'assessment area'." *Community Dividend*, Federal Reserve Bank of Minneapolis. March 8, 2018. <https://consumercomplianceoutlook.org/2010/first-quarter/cra-and-consumer-protection/>

Again, as in the case of the community development criteria, the ownership structure of the institutions this money is going towards is not specified. More surprisingly, the criteria do not specify or prioritize lending to people of color, despite the CRA's original advocates' goal of addressing redlining. It also does not place any emphasis on women, who have also historically been underfinanced.

Available data on national CRA lending unfortunately does not include categories beyond "small business," "community development," and "farm" loans. (Data on mortgage lending for CRA considerations is compiled under the Home Mortgage Disclosure Act.) The finest-grain data available is the amount of money lent to small businesses in low-income areas versus middle- and high-income areas and across population densities.<sup>71</sup> There is no information on the type of businesses, the business ownership structure, corporate affiliations (locally or non-locally incorporated and owned), or the demographic served beyond income level. The Dodd-Frank Act has required disclosure of the gender and race of small business borrowers; however, the data will not be available for a few years.<sup>72</sup>

<sup>71</sup> "CRA National Aggregate Reports." Federal Financial Institutions Examination Council. <https://www.ffiec.gov/craadweb/national.aspx>.

<sup>72</sup> Silver, Josh. "How Data Disclosure Will Help Prevent the Next Fi-



### Investing criteria

Diverging slightly from the focus on small businesses, farms, and homes, the focus of the investment category is on the level of qualified community development investments and grants, as well as the innovativeness and responsiveness of those investments and grants to the credit and community development needs of the community. Community development investments include those made in financial intermediaries (such as Community Development Financial Institutions and Small Business Investment Companies), nonprofit organizations (including CDCs), or direct investments in projects that work towards meeting the needs of LMI individuals.<sup>73</sup> This can include projects financed through the Low Income Housing Tax Credit and New Markets Tax Credit programs, which incentivizes investments in qualifying projects or CDCs.

### Services criteria

The service test has two categories for assessment: retail banking services and community development banking services. The first primarily examines the availability of branch locations and other financial services, such as ATMs and check cashing. The latter evaluates technical assistance, credit counseling, or participation on the boards of directors of community-based groups, local agencies, or intermediaries that help meet the credit needs of low- and moderate-income individuals or small businesses and farms. The community development services banks are encouraged to provide training to LMI individuals and community groups in the areas of “credit counseling,” “financial education or literacy,” or “foreclosure prevention.”

### Exams and examiners

The exams include the examiners’ assessments with

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nancial Crisis.” *Shelterforce*. February 23, 2017. <https://shelterforce.org/2017/02/23/how-data-disclosure-will-help-prevent-the-next-financial-crisis/>.

73 “Community Reinvestment Act; Interagency Questions and Answers Regarding Community Reinvestment; Guidance.” *Federal Register: Rules and Regulations*. Vol. 81, No. 142. Monday, July 25, 2016.

respect to the lending, investment, services, and community development tests. Despite being hundreds of pages long, the exams themselves do not usually provide extensive information on the types of loans, investments, and services that form the basis of an examiner’s analysis for a given rating (beyond the bucket categories of housing, small business, and farming), though some specific products or programs are often discussed and highlighted. The overall score that determines the final CRA rating is determined by a

### **Exams assess banks in three areas: lending, investing, and services. Revisions in the law adjusted exam requirements for banks according to their asset size.**

weighted sum of the points across all tests. With the lending test holding the greatest weight among the three, notably poor performance in the investment or services test can be outweighed by the lending test score.<sup>74</sup> This also tends to put more emphasis on low-income housing, small business loans, and community development loans over investments, grants, and other services. Discriminatory lending in itself—outside of the three separate tests—if identified by the regulator, can negatively impact the bank’s overall rating, and is summarized under the “fair lending” section of the CRA exam.

The exams also include the examiners’ consideration of a bank’s “performance context” which essentially takes into consideration the extent to which a bank can, given market conditions, safely and soundly perform its CRA functions, as well as the specific community development needs of the area. Examiners may include further considerations in exams in accordance with the “examinations procedures,” which are periodically updated. For large banks, such procedures provide further guidance on the evaluation of banks’

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74 Stegman, Michael. “Creating a scorecard for the CRA service test.” Brookings Institute. 2002.

performance on the lending, investment services, and community development tests.<sup>75</sup>

The examiners themselves come from a multitude of backgrounds—from the public and private sector, banks or community development organizations, legal work, or straight out of college from finance and accounting degree programs. Thus, the examiners' knowledge of community development best practices outside of what is stated in the Q&As or included in examiner trainings varies considerably. Examiners receive training at the agencies respective to the banks they will be examining—i.e. at the OCC, Fed, or FDIC. Though examiners have access to community development divisions of each of the agencies, at least at the Fed, the examiner training and community development divisions are to some extent functionally separate and often not well integrated.<sup>76</sup>

#### *Enforcement mechanisms*

The levers available to regulators when it comes to a bank's poor CRA performance are limited to the following (per the original statutory language):

- Denying an application for a national charter
- Denying deposit insurance for newly chartered state banks
- Denying an application for a branch
- Denying an application to replace a home or branch office
- Denying a merger with a regulated financial institution
- Denying the acquisition of shares of a regulated financial institution

This list notably omits any punitive repercussions for poor CRA exam results, either monetarily or through revoking a bank's charter status. Poor performance is generally considered to be a rating of "Needs to Im-

75 "Large Institution CRA Examination Procedures." The OCC, FRB, and FDIC. April 2014. [https://www.federalreserve.gov/supervisionreg/caletters/CA\\_14-2\\_attachment\\_1\\_Revised\\_Large\\_Institution\\_CRA\\_Examination\\_Procedures.pdf](https://www.federalreserve.gov/supervisionreg/caletters/CA_14-2_attachment_1_Revised_Large_Institution_CRA_Examination_Procedures.pdf)

76 Email correspondence with Ellen Seidman.

prove" or "Substantial Noncompliance," though CRA exams are taken into consideration in applications for mergers on a case-by-case basis, so such a rating does not guarantee mergers will be denied.<sup>77</sup> Moreover, 89 percent of banks evaluated in 2014 received a satisfactory rating while only 2 percent received a rating of "needs to improve," in what some have regarded as an issue of grade inflation.<sup>78</sup>

#### Gaps and opportunities for reform

The regulatory framework that has grown around the CRA in the last several decades has institutionalized the law across various agencies and put forward a broad range of criteria for defining community development and evaluating bank performance. This dispersion and flexibility within the criteria, examination, and enforcement structures present both gaps and opportunities for reform within the CRA regulatory framework. Reviewing these gaps and opportunities helps to identify the most important reforms to be made within the current regulatory framework as well as the extent to which the CRA can and ought to be reformed and used as a tool for community investment going forward.

#### *Definitions and criteria*

The fact that the Q&As outline many types of qualifying lending, investment, and service activities means that the law is flexible to a broad range of community development activities.

This flexibility means that there are opportunities to build on the definitions and criteria, but also means that the range of qualifying criteria can allow for banks to opt for the less involved, lower-impact projects, or projects that count as LMI investments but that may not necessarily provide a meaningful or lasting community benefit.

77 "CRA and Consumer Protection Issues in Banking Applications." *Consumer Compliance Outlook for 2010*. <https://consumercomplianceoutlook.org/2010/first-quarter/cra-and-consumer-protection/>

78 Silver, Josh. "The Community Reinvestment Act and Geography: How Well Do CRA Exams Cover the Geographical Areas that Banks Serve?" National Community Reinvestment Coalition. April 2017.

April de Simone of designing the WE, a community development lab based in the Bronx, points to an example in recalling the story of an International House of Pancakes franchise opening up in a low-income neighborhood.

“The Black entrepreneur was being celebrated for bringing this business in,” she recalls, “but you’re bringing it in an area where people are dying of obesity. We often like to fall into this trap of ‘let’s take the Black entrepreneur that rises out of the ashes of a traditionally disinvested area’ and we celebrate that one entrepreneur but we don’t want to look at the millions that didn’t get to that level. Is it about the entrepreneur or the millions that didn’t rise with the tides?”<sup>79</sup>

Drawing on the information gathered through designing the WE’s interactive “Undesign the Redline” exhibit and curriculum, Simone comments further on how businesses can be brought into neighborhoods via CRA financing without community involvement or ownership and end up not creating lasting community wealth.<sup>80</sup> Recalling how a grocery store was brought in as part of the new renaissance efforts in Harlem, she says, “Government and developers used this disinvested community, CRA dollars and subsidies came in to build a supermarket, and what did the community get back? They arguably got a place where they can shop, but what are the prices and what is the extra impact in the community? In a few years the store went bankrupt and all those public dollars went down the drain. The land was sold to a luxury developer. That huge potential asset is gone, essentially using CRA money to do that.”<sup>81</sup>

Simone contrasts this with the work of the People’s Community Market in Oakland, California, located in a community with a legacy of sharecroppers. “The community got tired of the narrative of being a food desert, so they got together and used a community equity shareholder model to raise \$1.5 million that was matched by an impact investment fund. How

79 Interview with April De Simone.

80 See <http://www.designingthewe.com/undesign-the-redline/> for more information.

81 Interview with April De Simone.

could CRA dollars go towards those types of projects that build shared value and wealth as opposed to the corporate model?” she asks.<sup>82</sup>

Concerns about gentrification and displacement have also emerged in light of the types of investments that can get prioritized under the CRA criteria, despite the inclusion of additional language to mitigate such effects. A 2016 report compiled by the National Community Reinvestment Coalition (the main policy advocacy organization for the CRA) notes that gentrification has been on the rise in metropolitan areas, offering economic revival to low- to moderate-income areas but also displacing lower-income renters as rents rise.<sup>83</sup>

**The range of qualifying criteria allow opportunities for banks to add new models, but can also allow them to opt for less involved, lower-impact projects that may not provide a meaningful or lasting community benefit.**

The Q&As specify that lending to high-income borrowers that end up displacing LMI people (and that is not included as part of a public sector or nonprofit development plan) does not qualify for CRA lending, and provides language advocating for the use of mixed-income housing. However, the report notes that “despite guidance by the federal bank agencies as to how banks can pursue mixed-income housing and avoid displacing lower-income residents from gentrifying neighborhoods, the role of banks in gentrifying neighborhoods appears to be rarely mentioned in CRA exams, in academic literature, or in articles

82 Ibid.

83 “The Community Reinvestment Act: How CRA Can Promote Integration and Prevent Displacement in Gentrifying Neighborhoods.” National Community Reinvestment Coalition. December 2016.

about gentrification.”<sup>84</sup>

Additionally, policy studies demonstrate that systemic barriers to lending in communities of color still remain. A 2004 report from NCRC compared lending in “minority and white” census tracts for the top 100 metropolitan areas. It found that “the percent of loans received by small businesses in minority census tracts declined as the level of African-American and white segregation increased,” concluding that “clearly, significant barriers remain in reaching small businesses in traditionally underserved communities.”<sup>85</sup> Though the Q&As specifically cite “minority- and women-owned financial institutions” as qualifying financial intermediaries for investment (the only time “minority” and

**Policy studies demonstrate that systemic barriers to lending in communities of color still remain. A 2004 report found that “the percent of loans received by small businesses in minority census tracts declined as the level of African-American and white segregation increased.”**

“women” are mentioned in the Q&As), people of color are not otherwise specifically mentioned, let alone prioritized, as part of the criteria.

*Agencies, exams, examiners and enforcement mechanisms*

With regards to the broader regulatory framework (i.e. the agencies, exams, examiners, and enforcement mechanisms), the dispersion of responsibilities across agencies and delegation to examiners present

<sup>84</sup> Ibid.

<sup>85</sup> “Inequalities in Small Business Lending by Income and Race of Neighborhood”. National Community Reinvestment Coalition. October 2004.

both gaps and opportunities. Arguably, the dispersion and institutionalization across agencies has protected the CRA from sweeping, dismantling changes. This distribution of authority further makes sense to the extent that each agency specializes in a certain type of financial institution. It also allows the CRA to be somewhat responsive to changes in the community development sphere by providing opportunities for coordination between communities and banks, as well as in updating the understanding of regulators, banks, and practitioners’ of current community development best practices.

For instance, for the last several years the Federal Reserve Bank of Kansas City has hosted a place-based program called Investment Connection. It began as essentially a mini-conference that brings together community groups, banks, and other funders to pitch projects that would be CRA-qualifying, with the goal of connecting banks and community development organizations with CRA-eligible projects. In addition to bringing together stakeholders, the events serve to close an information gap in communities, to educate the funding community about community issues and new projects seeking to address community development needs. In order to facilitate connections outside of these events, an online portal has been added.<sup>86</sup>

Similarly, the organizational and research activities of the agencies are an opportunity for communities and bankers to update and elaborate on community development best practices. Namely, the Federal Reserve, along with the other agencies, may host listening sessions to learn about challenges and opportunities facing CDCs or roundtables with financial institutions to discuss the types of development projects they should be focusing on.

Additionally, research publications on updated community development best practices are made available on the different agencies’ websites. For instance, a 2014 report from the Federal Reserve Bank of Dallas

<sup>86</sup> “Investment Connection Online FAQs.” Federal Reserve Bank of Kansas City. January 12, 2017. <https://www.kansascityfed.org/en/community/investmentconnection/resources/investment-connection-faqs>

states that “a new generation of community development models is emerging,” and cites the use of blending “people- and place-based strategies to realize a broader vision”—though such language has not yet been included in the Q&As.<sup>87</sup>

Meanwhile, examiner trainings and public comments on merger applications provide opportunities to identify and reinforce higher-impact projects and collaboration with communities. However, the extent to which community input and community development best practices make their way into CRA exams or reviews of applications for mergers varies. Throughout the examination process, the community has little involvement in determining the bank’s overall rating, in part due to the fact that the CRA exams are performed at inconsistent intervals and are announced via obscure formats.<sup>88</sup>

Comments can be provided on bank performance at any time and also on bank’s applications for mergers—but that requires knowing you have to go to the Federal Reserve’s website (for mergers) and the relevant agency’s websites for other comments. The comments that are made do, at times, have an impact on a bank’s ultimate rating, and communities are indeed active in providing comments and their own analyses for CRA exams.<sup>89</sup> However, it is difficult to tell from the CRA exam narrative if and how community comments informed the ultimate analysis.<sup>90</sup>

The performance contexts also provide an opportunity for community input, as examiners are required to discuss with community organizations how well

banks are meeting community development and financing needs. However, as Josh Silver of the NCRC has written, “the summaries [that end up in the final exams] are cursory and not informative.”<sup>91</sup> Moreover, while banks and community groups are allowed to submit their own performance context analyses to regulatory agencies, banks submit such analyses much more often than community groups, who “rarely” do.<sup>92</sup>

Meanwhile, the dispersion of regulatory authority and community development divisions across agencies and the delegation of authority to examiners can also result in inefficiencies and discrepancies in how banks are evaluated. For instance, reviews of community development best practices are conducted and researched by the various regulatory agencies and their regional offices, which may or may not result in consensus on community development best practices. Additionally, examiners compile a performance context analysis for each individual exam, though the performance contexts could be standardized at the interagency level by utilizing data already collected by the Census Bureau and incorporating community input on the community development needs for each region into this data.<sup>93</sup>

More generally, the rigor and transparency of the exams are points of concern. With regards to the examiners’ review of discriminatory lending, NCRC wrote in 2015 testimony that “even for the largest banks in the country, the fair lending section of the CRA exam reports in one to three sentences that the regulatory agency tested for evidence of illegal and discriminatory lending and that no such lending was found. There is no discussion of what precisely had been done to reach this conclusion.”<sup>94</sup> This lack of transparency provides “no evidence that the fair lending reviews conducted concurrently with CRA exams are

87 Blum Sobel, Elizabeth. “Healthy Communities: A Framework for Meeting CRA Obligations.” Federal Reserve Bank of Dallas. March 2014.

88 Silver, Josh. “CRA Performance Context: Why it is important for Community Development and How to Improve It.” National Community Reinvestment Coalition. 2016. “Performance Evaluation: Facilitation Public Input on CRA via Federal Agency Websites.” National Community Reinvestment Coalition. 2016.

89 Silver, Josh. “CRA Performance Context: Why it is important for Community Development and How to Improve It.” National Community Reinvestment Coalition. 2016.

90 Taylor, John and Silver, Josh. “The CRA: 30 Years of Wealth Building and What We Must Do To Finish the Job.” Chapter in *Revisiting the CRA: Perspectives on the future of the Community Reinvestment Act*. Federal Reserve Banks of Boston and San Francisco. February 2009.

91 Silver, Josh. “CRA Performance Context: Why it is Important for Community Development and How to Improve It.” National Community Reinvestment Coalition. 2016.

92 Ibid.

93 Ibid.

94 “Testimony of Josh Silver, Senior Advisor, NCRC Regarding the Regulatory Review Mandated by the Economic Growth and Regulatory Paperwork Reduction Act (EGRPRA).” National Coalition for Community Reinvestment. December 2, 2015.

rigorously testing for abusive, discriminatory, and illegal lending.”<sup>95</sup> Beyond the fair lending section of the exam, studies have shown that the “quantitative criteria are applied in an inconsistent manner on CRA exams, suggesting that a number of CRA exams have ratings that cannot be justified.”<sup>96</sup>

Similarly, the ratings scale makes it difficult to provide accountability for areas of improvement within the exam that are not reflected in the overall score. Moreover, with the numerical score of the exam being based on a 24-point rating system, distinguishing among the banks that receive a “satisfactory” rating is difficult. “Even if you’re going to pass 89% of banks as satisfactory, how are you going to differentiate among them?” Josh Silver of NCRC asks. “In that big of a bucket you’re going to have an A versus a B or C.”<sup>97</sup>

Meanwhile, the enforcement mechanisms are arguably no longer stringent enough to induce better performance on the CRA. As Robert Kuttner, co-editor of *The American Prospect* and former Senate Banking Committee staff member who played a key role in drafting the CRA, notes, “a lot of the levers we had in the 1970s with the CRA have gone away because so much of banking is deregulated.”<sup>98</sup> In addition to the expansion of financial activity outside of CRA-covered institutions that has diminished the relative scope of the CRA, the enforcement mechanisms of denying applications for mergers and expansions may not adequately incentivize the banks that have the greatest impact and systemic significance in the current economy.

The main repercussion for the largest banks when it comes to poor CRA performance is negative press. However, since many of these banks already hold significant market shares in communities, their proximity and convenience can outweigh communities’ con-

cerns for poor CRA performance. Moreover, a poor CRA performance sometimes provides a marketing opportunity for the banks to capitalize on the trending issue of the times—as opposed to addressing their systemic impacts.

Me’Lea Connelly, Director of the Association for Black Economic Power, comments on how this allows banks’ CRA focus to shift with what’s trendy. “Wells Fargo failed its CRA, so now they say they’re going to give to a Black Lives Matter platform—it lets [the banks] pivot to whatever pain point *they* created in the world,” she observes.<sup>99</sup> Calling this phenomenon “triple dipping,” she argues that “the banks give back to the community and they get public relations credit for that, they get credit for supporting diversity so they can pull that card and get out of being criticized, and they’re making a profit on all of that in the process. It’s creating a punishment for themselves that ends up benefiting them.”<sup>100</sup>

Additionally, as online and mobile provision of financial services becomes increasingly ubiquitous, branch locations increasingly are being considered solely from a profit and marketing standpoint, rather than from the perspective of meeting the credit needs of local communities. Branch closings have continued to negatively affect particular localities, especially rural areas.<sup>101</sup> A branch closing creates a serious credit need for populations distanced either economically or physically from the availability of online and mobile banking. While there is an opportunity for CRA-covered online banks to reach rural populations, the extent to which they will take on this role remains to be seen.

Ultimately, be it through the breadth of the definition and criteria, the lack of coordination and centralization on the examination side, or the broader issue of the growing consolidation of banks and their increas-

95 Ibid.

96 Taylor, John and Silver, Josh. “The CRA: 30 Years of Wealth Building and What We Must Do To Finish the Job.” Chapter in *Revisiting the CRA: Perspectives on the future of the Community Reinvestment Act*. Federal Reserve Banks of Boston and San Francisco. February 2009.

97 Interview with Josh Silver.

98 Interview with Robert Kuttner

99 Interview with Me’Lea Connelly

100 Ibid.

101 “Bank Branch Closures from 2008-2016: Unequal Impact in America’s Heartland.” National Community Reinvestment Coalition. 2017. [https://ncrc.org/wp-content/uploads/2017/05/NCRC\\_Branch\\_Deserts\\_Research\\_Memo\\_050517\\_2.pdf](https://ncrc.org/wp-content/uploads/2017/05/NCRC_Branch_Deserts_Research_Memo_050517_2.pdf)

ing centrality in the economy limiting the strength of the CRA's enforcement mechanisms, banks by and large continue to pass their CRA exams with satisfactory or better ratings. As Richard Marsico writes in his book *Democratizing Capital*, “the federal agencies that enforce the CRA are so fearful of allocating credit that they use vague and subjective criteria for evaluating bank lending, making it difficult to hold a bank accountable for a poor lending record or even to know what constitutes a poor lending record.”<sup>102</sup>

While it is indisputable that the CRA has induced billions of dollars to be reinvested into communities, it is not nearly harnessing the full capacity of today's financial sector, and even CRA-covered lenders could certainly be doing significantly more for communities given their immense capacity. As Grzywinski says, “if you consider the number of bank branches around the country and consider their community presence, and then compare that to CDFIs and how relatively little they have in terms of resources, the banks' argument [that they're fulfilling the CRA through such investments] is nonsense. They're not meeting the credit needs of their service areas.”<sup>103</sup>

Over the years, many important reforms have been proposed to address insufficiencies that have emerged as the financial services industry evolved and as communities gained more experience with the law and how it should meet their needs. Such proposals focus on increasing the overall transparency and rigor of the law by enhancing data requirements, improving avenues for community input on the exams, increasing the number of ratings, and even expanding the law by either redefining assessment areas or to apply it to other financial institutions such as credit unions and mortgage affiliates. All are important reforms that would help strengthen the CRA.

There is a set of reforms, however, that is currently receiving little attention. These reforms would include additions to the Q&A criteria or even changes to the

definition of community development to center the law more within “a new generation of community development models” that focuses on “people- and place-based strategies to realize a broader vision,” as mentioned in the 2014 Dallas Federal Reserve report referenced earlier. Such models could include a range of community wealth building approaches and institutions. What these models would entail and their imperative in light of the structural, ideological, and legislative changes that have occurred over the last several decades is considered in Part 2.

**There is a set of reforms that is currently receiving little attention. These reforms would center the law more within “a new generation of community development models” that could include community wealth building approaches.**

Putting pressure on regulatory agencies to play a greater role in coordinating between communities and banks, and elevating the emphasis of such projects, would help facilitate their implementation. Equally important novel reforms include the enactment of stricter penalties for low CRA ratings to better incentivize higher impact projects and expanding the CRA to apply to more types of financial institutions *specifically by asserting a more fundamental “public purpose” obligation* (similar to those required in some utility and service industries). That would go farther in justifying and sustainably instituting an expansion of the CRA than legal justifications in prior proposals.

Such legislative and regulatory changes, along with the prior reform proposals that are most pertinent to making the CRA an effective tool for community wealth building, are discussed in detail in Part 2.

102 Marsico, Richard. “Democratizing Capital: The History, Law, and Reform of the Community Reinvestment Act.” *New York Law School Law Review*. Vol. 49. March 14, 2005.

103 Interview with Ron Grzywinski

## Part 2: CRA reform and community wealth building

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### The design challenge of system change and barriers to reform

In The Democracy Collaborative’s 2015 report *Cities Building Community Wealth*, Marjorie Kelly and Sarah McKinley highlighted the design challenge for community developers in the present political economic paradigm, asking, “Can we create an economic system—beginning at the local level—that builds the wealth and prosperity of everyone?”

The question they pose is a response to growing recognition that the current political economic system has largely fallen short of bringing about equitable and sustained prosperity over the past several decades. For example, they note that real wages for the bottom 80 percent of Americans have stagnated in the last 30 years, while income for the top 1 percent has doubled since 1980. This growing inequality has disproportionately affected communities of color, with racial wealth disparities nearly doubling over the same period.<sup>104</sup> Perhaps unsurprisingly, those at the bottom experience the greatest economic insecurity and are hardest hit by the national and global economic forces that produce recurrent financial crises and recessions. However, middle-class Americans are not immune to

the growing economic challenges, as evidenced by the fact that upward mobility is becoming increasingly difficult.<sup>105</sup> And, of course, climate change presents the potential for severe economic dislocations and pressures, the majority of which will likely be felt most by low- and middle-income communities.

These inequities and lack of economic security have emerged and deepened despite the fact that the “free market” is purported to efficiently bring about greater opportunity, prosperity, and freedom of the whole. The failures and shortcomings of markets to deliver on these goals necessitates economic policies to fill in the gaps, and these can be a vital lifeline for communities disserved by or otherwise unable to access the gains of the market. Yet ultimately such policies often face significant barriers to more fully meeting the needs of the communities they intend to serve, to say nothing of actually changing the structural dynamics that perpetually undermine their aims. The CRA is a good example of this. It has overseen the reinvestment of billions of dollars of capital into com-

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104 Pathe, Simone. “Today’s racial wealth gap is wider than the 1960s.” *PBS NewsHour*. February 18, 2015. <http://www.pbs.org/newshour/making-sense/todays-racial-wealth-gap-is-wider-than-in-the-1960s/>

105 “Weathering the recession: The financial crisis and family wealth changes in in low-income neighborhoods.” The Annie E. Casey Foundation & Urban Institute. March 2012. <http://www.urban.org/sites/default/files/publication/25686/412626-weathering-the-recession-the-financial-crisis-and-family-wealth-changes-in-low-income-neighborhoods.pdf>. Inskeep, Steve. “Top 20 Percent of Americans ‘Hoard the American Dream.’” *National Public Radio*. May 31, 2017. <http://www.npr.org/2017/05/31/530843665/top-20-percent-of-americans-hoard-the-american-dream>.



munities. However, structural and ideological barriers remain in the way of reforms that would both allow the law to better serve communities and, over time, fundamentally alter the nation's financial system such that the CRA's gains are not undermined.

These same barriers are what have driven many communities across the country to turn to themselves for solutions, to seek out new models and approaches for economic development and to democratize ownership and wealth at the local level. This experimentation in new wealth building models and strategies is, in part, what the 2014 Dallas Federal Reserve report mentioned in Part 1 referred to as “a new generation of community development models.”<sup>106</sup> Consciously or unconsciously, such efforts are also laying the groundwork of system change—i.e. a “new normal of political-economy activity” that is “place-based, inclusive, collaborative, and ecologically sustainable.”<sup>107</sup>

These wealth building models are a central component of the broader vision and conversation around system change that has emerged in recent years, especially since the 2007-2008 financial crisis. The significance of such bold visioning is, on the one hand, strictly logical: no one political economic system has existed in perpetuity. On the other hand, it is an acknowledgement that from the political and economic disruptions and inequities posted by climate change, to recurrent economic crises, rampant inequality, uneven economic development, and political stalemate, the current system is under increasing stress.

However, the barriers to advancing a system change agenda are significant. These include: (1) numerous structural barriers, i.e. institutionalized economic and political arrangements, both domestic and international, that have been further solidified over the last several years, impeding effective policy reform, and (2) a pervasive free-market orthodoxy motivating, justifying, and perpetuating the structural status quo,

particularly in the U.S. Given these two interrelated sets of barriers, efforts to fundamentally restructure the functioning of private institutions, especially private financial institutions, are severely hindered from entering public discourse, no less existence.

**Structural and ideological barriers have driven many communities across the country to turn to themselves for solutions, to seek out new models and approaches for economic development.**

What might be some of the reforms that will allow the CRA to overcome these barriers and realize its systemic change potential? The aim in reviewing these barriers here is to understand what a piece of legislation that seeks to transcend these barriers (in this case, a modern CRA) might or even could look like, to understand the limitations but also the previously unexplored system-changing opportunities it presents. It further highlights the necessity of community wealth building approaches, discussed in greater detail in the next section. Understanding how and to what extent the CRA can be made a tool for community wealth building models and approaches is the focus of the remainder of Part 2.

The related proposals build on reforms that have been consistently put forward, including the fundamental reform of extending the CRA beyond depository institutions and bank branches. However, in recognizing that barriers to such fundamental reforms may persist and more generally that the CRA is just one policy tool among many that may facilitate system change, a brief discussion is provided of tools and policies to be advocated alongside CRA reforms.

106 Blum Sobel, Elizabeth. “Healthy Communities: A Framework for Meeting CRA Obligations.” Federal Reserve Bank of Dallas. March 2014.

107 Kelly, Marjorie and McKinley, Sarah. *Cities Building Community Wealth*. The Democracy Collaborative. November 2015, 2; 12.

### *Structural barriers: domestic and international factors*

Over the last several decades, a number of structural barriers have prevented the comprehensive systems approach described above. Deregulatory policies, institutional and asset rearrangements, and growing international pressures have led to increased consolidation of power and capital. Most notably, since the 1970s, corporate America—both its workers and managers—experienced a remarkable restructuring. While “welfare capitalism” reigned in the 1950s through the 1960s, providing stable long-term jobs to low-skilled workers supported by strong unions, the 1970s through 1980s saw

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the dismantling of this framework, including the displacement of the managers, unions, and workers that composed it.

In her book *Liquidated: An Ethnography of Wall Street*, author Karen Ho attributes this restructuring to an express effort on the part of Wall Street banks—in part spurred by global economic pressure following the oil crisis—to displace what they saw as inept managers and to discipline ‘bloated’ corporate conglomerates. This was accomplished by aligning corporate success with its stock price (a.k.a. shareholder value), privileging profit maximization over other functions. In more than 100 interviews with Wall Street bankers, Karen Ho documents how the banks used junk bonds to buy up corpora-

tions, break them up along business lines, supplant their management and owners, and resell the pieces through initial public offerings (IPOs) to drive up stock value.<sup>108</sup>

Policy changes beginning in the late 1970s also supported this structural transition, as Reagan-era legislation reworked rules regarding labor, trade, and growth in the name and interests of the free market.<sup>109</sup> Despite the purported hope that placing greater faith in the market would fulfill the promise of freedom and prosperity for all, the resulting restructuring of the economy has only consolidated ownership and wealth into a smaller and smaller subset of the population. The 1970s-on saw a remarkable uptick in the share of assets (i.e. stocks, property, and savings) held by the top 1percent, which had steadily declined in preceding decades following New Deal-era legislation. For instance, the share of national income of the top 0.1 percent spiked, real wages declined as productivity increased, and tax rates on the highest income brackets and corporations fell precipitously.<sup>110</sup> This accumulated wealth among individuals and corporations in turn has translated to political power in the form of super PACs, private campaign contributions, regulatory capture, and the revolving door between Congress and the private sector, that has weakened the inequality-mitigating infrastructure of the welfare state.<sup>111</sup> Moreover, the systematic criminalization and incarceration of African Americans with the transition from Jim Crow to the War on Drugs during this same time period overtly marginalized

108 Ho, Karen. *Liquidated: An Ethnography of Wall Street*. (Duke University Press. 2009), 122-164.

109 Harvey, David. *A Brief History of Neoliberalism*. (Oxford University Press. 2005), 1

110 Harvey, “A Brief History of Neoliberalism,” 16, 25-26.

111 Palmer, Maxwell and Schneer, Benjamin. “Capital Gains: The Returns to Elected Office from Corporate Board Directorships.” *The Journal of Politics*. Vol 38(1). January 2016. Carnes, Nicolas. “Does the Numerical Underrepresentation of the Working Class in Congress Matter.” *Legislative Studies Quarterly*, Vol 37(1). February 2012. Kirkpatrick, David. “Does Corporate Money Lead to Political Corruption?” *The New York Times*. January 23, 2010. Hacker, Jacob and Pierson, Paul. “How Washington Has Made the Rich Richer – And Abandoned the Middle Class.” *Scholars Strategy Network: Key Findings*. October 2011.

and suppressed the political participation of a significant portion of the American population.<sup>112</sup>

Meanwhile, the international pressures of post-war economic liberalization and the rise of global competitors increasing since the 1970s has also pushed national economic policy to favor capital over labor. In particular, some research suggests that as capital has become more mobile (more able to move across national borders) and more central to the U.S. economy, the threat of capital flight (financial capital rapidly leaving domestic markets) has further dissuaded anti-capital policy (e.g. higher corporate or higher income taxes), with deleterious effects on the capacity of the welfare state.<sup>113</sup> In this sense, beyond the endogenous factors associated with the further integration of the private sector and government, policymakers are increasingly trapped into a pro-capital policy due to international competition for capital (or at least are deterred from implementing anti-capital policy). The lack of investment in or emphasis on public education policy towards more innovative and sustainable sectors has arguably worsened the long-term economic competitiveness of the country internationally and wealth inequality divides domestically.

#### *Free-market orthodoxy compounds structural barriers*

As these structural changes have allowed the market to play an increasingly central role in the global and domestic economy, public and policymaking discourse in the U.S. can often become locked into a false debate about government intrusion into a “free market,” presenting a further barrier to effective system changing economic policy. The rhetoric of “the free market” suggests that (1) there is an independently operating market of freely enterprising private actors and (2) that any government involvement is an exogenous intervention on this free functioning. That is, there is

a notional separation between “the government” and “market.” Consequently, government intervention in the form of policy action is deemed permissible only to address “market failures,” or specific instances where the market produces an “inefficient” outcome. If the government “intervenes” beyond addressing these failures through legal enforcement or pro-social economic policies, it is considered to have burdened the market to a point of producing a social cost.<sup>114</sup>

This artificial separation between the market and government persists despite the fact that economic theorists going back to Adam Smith have acknowledged and argued that government has a critical role in establishing laws enforcing essential components of market functioning.<sup>115</sup> Thus, the market can be seen as being dependent on the government because the government provides legal support to the fundamental components of free-market functioning. Not to mention, a network of laws helps maintain trust and functionality in the economic system—such as FDIC insurance in the case of the banking system.

These two sets of barriers to system change—structural changes towards privatization and wealth concentration occurring since the 1970s and free-market ideology—do not operate independently; adherence to the notion of the free market is not just galvanizing campaign rhetoric but is also to some degree core to the actions of private actors shaping the structural determinants of the present system.

Karen Ho, for instance, finds that the motivation to align corporate success with stock price stemmed from cooptation of economic theorists of the 1960s and 1970s (i.e. Chicago school economists) who attempted to extend Smith’s theory that the efficiency of markets arises from small business owners having a unique direct governing and ownership relationship with their profits and private property. These neoclassical (i.e. free-market) economists theorized that the

112 See *The New Jim Crow* by Michelle Alexander.

113 Rodrik, Dani. “Has Globalization Gone Too Far?” (Institute for International Economics. 1997). 49-55. Hays, Jude. “Economic Globalization and Domestic Politics in Developed Democracies.” Chapter in *Globalization and the New Politics of Embedded Liberalism* (Oxford University Press. 2009).

114 Reich, Robert. “Saving Capitalism” (Alfred A. Knopf. 2015), 1-7.

115 Cairns J.W. “Adam Smith and the Role of the Courts in Securing Justice and Liberty” in Malloy R.P., Eversky J. (eds) *Adam Smith and the Philosophy of Law and Economics*. Law and Philosophy Library, vol. 20 (Springer. 1994), 31-61.

conduit through which to collapse governance, ownership, and profits in the modern context could be the shareholder, as opposed to the individual entrepreneur. Through her interviews, Ho chronicles how the idea extended beyond the sphere of academia and in the heart of the market itself as Wall Street banks adopted this as justification for their restructuring of corporate America to align company value with stock price.<sup>116</sup>

Under Ho's analysis, such a market-centric logic resembles a self-fulfilling closed feedback loop, creating a disconnect between the structural arrangements and actions of these market actors and the market outcomes they produce. While she was speaking specifically to cycles of booms and busts, other market outcomes can similarly be seen under this logic as random aberrations or natural consequences as opposed to endemic, systemically produced dysfunction. One of the most prevalent of these endemic dysfunctional market outcomes, of course, is extreme wealth inequality; another is ecological destruction and despoliation.

#### *The upshot for system-changing policy: Limitations and opportunities*

The ultimate upshot of these structural and ideological barriers is that effective economic policy, i.e. what would really be necessary for those marginalized by the present system, are severely restricted from conversation and existence. With the government notionally relegated to playing a relatively marginal role in market functioning, the market is left to perpetuate and exacerbate its shortcomings. That is, with the ideological false-antithesis of "government vs. market" now well established (be it in business schools, political rhetoric, or public discourse, etc.), economic policies that attempt to correct these glaring systemic dysfunctions are seemingly precluded from debate.

Moreover, the institutionalized alignment of policy with market interest in recent decades, the ongoing influence of elite interests on Capitol Hill, and the

subsequent revolving door between private and government institutions (especially Wall Street, Congress, and corporate America), has obstructed the government's ability to seriously interrogate and redefine its role in the market-dominated economy, and has seriously weakened its responsiveness to public concerns on this matter.

The consequences of these barriers to system changing policy reform is that those at the bottom—those lacking the economic or social capital to become market participants beyond consumers—continue to face an increasingly grave Catch-22 dilemma inherent in the system. Their lack of resources disallows their ability to engage with or gain from the market while at the same time the fact that they present little value prospect to the market inhibits the market from naturally expanding outward to them. Increasingly, even those in the middle remain trapped towards the bottom, as social stratification has increased and upward mobility within the middle class has diminished.

The design challenge initially posed then, in this sense, entails not only addressing wealth inequities—"can we create an economic system that builds wealth and prosperity *for everyone?*"—but also creating for individuals greater economic security and bringing them greater control over their economic prospects through the democratization of ownership and governance at every level, beginning locally. For communities and community developers this means identifying models and methods that work to ensure greater collective ownership, wealth, and governance opportunities.

For federal economic policy in the 21<sup>st</sup> century there lies an even more fundamental need to move the national dialogue beyond the false antithesis and false dichotomy of "market" and "government"—to reassert a more fundamental public obligation of private banks or to increase the role of publicly owned institutions—and to better align economic policy with the community wealth building framework in order to more fully support communities in this effort.

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116 Ho, Karen. *Liquidated: An Ethnography of Wall Street* (Duke University Press. 2009), 173.

## Advancing the community wealth building model

The structural changes in the economy occurring over the past several decades, the growing market ideology motivating it, and the severe limitations of federal policy to address the root of the country's most endemic issues has led communities and community developers to ask the question: "Can we create an economic system—beginning at the local level—that builds the wealth and prosperity of everyone?"

This question is certainly not new. In one form or another it has continued to be the question at the root of economic policies and community efforts over the last several decades, including, as we have seen, the Community Reinvestment Act. However, some activists, organizers, and theorists are taking it one step further and approaching the question through the lens of the design challenge of system change. This is in part a recognition that many of the traditional responses endeavored thus far have, at best, held the line against further deterioration of social, economic, and environmental trends and at worst perpetuated or exacerbated them.

In particular, TDC's *Cities Building Community Wealth* report discusses community development practices that all too often put faith in private or corporate interests to build wealth. This approach, however, continues to consolidate wealth and power into the hands of the few rather than the many, and has created systemically significant institutions, particularly financial institutions, that helped bring about a devastating financial crisis. Furthermore, the power and influence of these large profit-maximizing corporations and financial institutions dissuade genuine democratic political and economic participation at all levels. Thus the *Cities Building Community Wealth* report builds on and links experiments and developments on the ground to a vision of a new political economic system that embodies an inclusive, community-focused approach over profit maximization and growth-for-growth's-sake.

By bringing attention to investments, and lack thereof,

in low- and moderate-income (LMI) communities, the Community Reinvestment Act has significantly impacted the scale and trajectory of the community development field in recent decades. However, new approaches like those detailed in the *Cities Building Community Wealth* report—and now more widely understood by community developers and regulators to entail "a new generation of community development models"—have yet to make their way into the CRA regulatory framework to become more central to CRA-related loans, services and investments than the traditional approaches.

The heart of the problem with the 'traditional approach' to community development is the heightened reliance on incentives (including subsidies and tax

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abatements) to draw national or multinational firms into local economies in an effort to further community revitalization. Despite the stated goal of economic development, this approach, and the way it is executed, works "toward a different set of outcomes" as the report highlights.<sup>117</sup> Though many cities and economic developers have taken up a "new framework for inclusive economic development," this traditional approach still predominates and has been growing.<sup>118</sup> For instance, city governments dramatically increased their use of incentives for corporate investment be-

117 Kelly, Marjorie, and McKinley, Sarah. *Cities Building Community Wealth*. The Democracy Collaborative, November 2015, 13, 26.

118 Ibid.

tween 2004 and 2009. Meanwhile, support for community development corporations, community development loan funds, job training, and economic development budgets dropped drastically.<sup>119</sup>

Relying on corporate development is problematic for several reasons. First and foremost, the expected economic benefits of a corporate relocation or a new facility often are not realized and are sometimes outweighed by the costs. Examples of companies extracting millions in incentives only to fail to deliver the promised number of jobs (or quickly lay off the workers hired) are commonplace.<sup>120</sup> Secondly, it allows

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corporations to play one locality off against another. As has been demonstrated many times, corporations will leave one community to get bigger subsidies from another, or threaten to leave in order to extract more incentives from their home community. In essence, it is a “beggar thy neighbor” approach that opens the door for businesses to blackmail local communities.<sup>121</sup>

Another problem is that the community does not own the assets. Rather, absentee owners—the shareholders and executives of companies living outside of communities—control the assets.<sup>122</sup> This includes the way the assets are used, whether or not the assets stay in the community or are moved to someplace with lower property tax or weaker unions, etc. Though some jobs

may be created and a sole franchiser gains ownership of assets, the community’s local economy is dependent on the whims of that national corporation’s success and interests. Meanwhile, profits are generally not re-directed back into communities, but to the national corporation (and its elite shareholders) while workers are subject to the wage, training, and participation standards of the company, which may or may not be satisfactory to the needs of the community.

This process, as a whole, often lacks the inclusive and collaborative input of the community, thereby perpetuating the already pervasive systemic barriers to employment, asset ownership, and wealth faced by those marginalized by the present system. Politicians, while nominally beholden to local constituents, often pursue such deals behind closed doors with little real input from community residents or community development experts. The option for the public at large to more fully participate in the economic system as a means to grow wealth is also made further out of reach as large corporations are prioritized over small- and medium-sized, locally owned firms. Various studies have shown that as firm size has grown, share ownership of publicly traded firms has consolidated into the top 10 percent of society, and corporations are increasingly allowing share prices to rise to a level out of reach of public investment.<sup>123</sup>

An alternative framework focuses on the return of ownership and control to communities building up from the local level. As Kelly and McKinley note, “ownership of assets is the foundation of every economy, for it determines who has control and who receives the lion’s share of benefits.”<sup>124</sup> Thus for communities seeking inclusive development, “the essential tool is transferring ownership, so the benefit of the assets stays in the community” as Ed Whitfield, co-managing director of the Fund for Democratic Communities, comments for the report.<sup>125</sup> This shift in the structural arrangement of ownership and con-

119 Kelly, Marjorie, and McKinley, Sarah. *Cities Building Community Wealth* (The Democracy Collaborative, November 2015), 26.

120 Kelly, Marjorie, and McKinley, Sarah. “Incentive wars” in *Cities Building Community Wealth* (The Democracy Collaborative, November 2015), 30–31.

121 Kelly and McKinley, “*Cities*,” 29–30.

122 Kelly and McKinley, “*Cities*,” 31.

123 Holm, Erik and Eisen, Ben. “Amazon’s brush with \$1,000 signals the death of the stock split.” *The Wall Street Journal*. March 26, 2017.

124 Kelly and McKinley, “*Cities*,” 19

125 Ibid.

trol of assets, from ownership and control by a few to ownership and control by many, and the intentional inclusion of traditionally marginalized groups, is imperative to shifting to an economic system that builds wealth and prosperity more equitably and sustainably.

Thus, an aim of the community wealth building framework is to build broad-based ownership, not through incentivizing disparately owned assets by individual entrepreneurs, or consolidating wealth opportunity in the stock markets, but by increasing the inclusive and collective ownership of assets by local residents. Some of the institutional models and policy tools already being used to achieve this end include social enterprises, community development corporations, employee stock ownership plans (ESOPs), municipally owned enterprises, community land trusts, and perhaps most importantly, cooperatives, in which all members have one share and one vote.

Importantly, such models also have a long history in communities of color. In her book *Collective Courage: A History of African American Cooperative Economic Thought and Practice*, author Jessica Gordon Nembhard chronicles the use of cooperatives (including credit unions) by the Black community as part of post-Civil War reconstruction efforts, throughout the Great Depression, and during the civil rights movement.<sup>126</sup> Organizations like the Federation of Southern Cooperatives Land Assistance Fund continue this legacy today. Increasingly, cooperatives serve as economic security for immigrant communities as well; the third largest worker cooperative in the US, Si Se Puede of Brooklyn, N.Y., was founded to provide immigrant women with living-wage jobs as well as social support and training opportunities.<sup>127</sup>

The development of these inclusive business models and their use alongside other key community institutions, both private and public, is important to creating

a new, mutually supportive system. This goal also requires cross-sector collaboration and utilizing place-based assets such as social networks, the existing infrastructure, local culture and ecology, and anchor institutions, including hospitals and school systems. By bringing everyone to the table to determine the resources necessary (workforce training, investments, etc.) and identify underutilized assets, the approach works to create a new normal of economic activity that supports more equitable development. Ultimately, rather than subsidizing the entry of large corporations and outside developers and planning new developments behind closed doors, greater collaboration among local institutions keeps resources circulating locally, creating a multiplier effect—e.g. a local small business or cooperative sells to local hospitals, universities, and city government, which creates stable and increased employment, which in turn increases tax revenue and local spending, which can then be used to fund social services or further equitable local economic development (which will generate further employment and revenue, and so on).

Developing this system, by necessity, must begin at the local level. History has shown that the current political economic system is generally unable and unwilling to redistribute wealth and asset ownership. The question then becomes, who sparks that dialogue to bring everyone to the table on the local level? On the one hand, in many communities, this process has started organically, as those marginalized or concerned by the present system have turned to themselves for solutions to provide greater wealth opportunity, stable employment, and ecological sustainability. For many communities, the community wealth building framework is useful to begin thinking differently about community development best practices and sparking conversations among community developers in nonprofits, private institutions, city governments, and regulatory agencies.

On the other hand, a vast framework of federal policies has worked to shape community development efforts in communities over the years. As discussed above, the Community Reinvestment Act is promi-

126 Gordon Nembhard, Jessica. *Collective Courage: A History of African American Cooperative Economic Thought and Practice* (The Pennsylvania State University Press. 2014).

127 Reme, Monika. "Immigrant Workers are Using Co-ops Like a Boss." *Bedford & Bowery*. August 5, 2016. <http://bedfordandbowery.com/2016/08/immigrant-workers-are-using-co-ops-like-a-boss/>.

ment among these policies, channeling funds into community development efforts through an evolving regulatory framework that elaborates on and implements the original language of the Act. However, and again as previously noted, there are many gaps in the current regulatory framework, including that the qualifying criteria do not currently encourage wealth building strategies that feature community ownership and control. More generally, with the immense expansion of financial activity being performed outside of depository institutions and bank branches and the limited enforcement mechanisms available to regulators, the CRA is not nearly meeting its full potential, nor are banks using their immense capacity to more fully meet the credit needs of the communities they operate in.

Meanwhile, the billions of dollars that *are* going towards CRA-related community development investments largely are not going towards the type of community development models that might more effectively keep wealth in communities and more equitably distribute wealth. In a search of the most recent CRA exams of the top 10 commercial banks by asset size (as of September 2017)—the words “co-op”, “co-operative”, “land trust”, “social enterprise”, and even “mixed income” (which is specified in the Q&As) were completely absent.<sup>128</sup> The word “collaborative” appeared a total of 4 times. This indicates that while at least small businesses remain a core component of CRA assessment, the particular community wealth building models are not currently a focus of the assessment and the activity of banks with the greatest capacity and resources.

While some capital from the largest commercial banks is undoubtedly making its way to such community wealth building models, either through the work of CDCs and CDFIs or investments or grants going

directly towards community development projects, assessing the impact of such investments remains difficult given the exam narrative (and indeed the impact of CDFIs and CDCs in communities can vary). With respect to CDFIs, Mark Pinsky, President & CEO of Opportunity Finance Network (the national trade association for CDFIs) from 1995–2016 and now president and CEO of Five/Four Advisors, recalls that “CDFIs were created to finance, in a sense, alternative and fringe economies” that emerged in the 1970s and 1980s.<sup>129</sup> However, throughout the 1990s and into the mid-2000s following the establishment of the CDFI Fund in 1994, “CDFIs took on a role of linking to the mainstream.” More recently—and barring significant exceptions—Pinsky notes that “overall, as a trend, the CDFI industry has drifted from being effective [in communities] to making the [traditional] market work. Instead of being advocates for the communities they serve, they have to a greater extent become an instrument of the financial service industry and government.”<sup>130</sup>

There are, of course, exceptions to this trend, and to the extent that community development best practices continue to be updated to include more community wealth building approaches, CDCs, CDFIs, and other development organizations remain a valuable tool for building up and supporting such approaches. There are several CDFIs and development organizations that specifically focus on cooperative development and lending, such as The Working World, Shared Capital Cooperative (a cooperative loan fund and CDFI), the Cooperative Fund of New England, the Local Enterprise Assistance Fund, Cooperative Development Services, and the Federation of Worker Co-ops. The growing awareness of other community development models, such as community land trusts and social enterprises, is helping communities and regulators realize the greater potential of these models to equitable and sustainably build wealth.

Moreover, some CRA-regulated banks are indeed explicitly lending to community wealth building ap-

128 Banks selected from the Federal Reserve Statistical Release list of Large Commercial Banks (as of September 30, 2017). <https://www.federalreserve.gov/releases/lbr/current/>. Exams were collected from the OCC website, Federal Reserve website, and company website in the case of Bank of New York Mellon. Most exams were from the years 2009, 2012, or 2013. The words “CDC” and “CDFI” were much more consistently cited, with multiple mentions on several of the exams.

129 Interview with Mark Pinsky

130 Ibid



proaches and institutions. Most notably, the National Cooperative Bank (NCB) is a deposit-taking institution (originally founded by congressional mandate in 1978 and later privatized as a cooperatively owned financial institution in 1981) that focuses on lending to cooperatives and low-income communities nationally. In its most recent exam the bank received recognition for supporting cooperative development in LMI communities (discussed more in the next section).<sup>131</sup>

### *The imperative of re-envisioning the CRA as a tool for system change*

Despite the growing acceptance of the community wealth building framework and the opportunities within the CRA to utilize such approaches, however, the system-changing potential of the CRA is going underutilized. Meanwhile, banks are often still not consistently or fully meeting the credit needs of communities.

Me’Lea Connelly, director of the Association for Black Economic Power, offers a stronger critique, arguing that the CRA as policy at the highest level can be seen as perpetuating a broader system largely unconcerned with and not adequately meeting community investment needs. “We can’t talk about [the CRA] without talking about who it’s benefiting and why it exists,” she argues. She continues:

The CRA is an attempt to correct the insidiousness and flaws of capitalism. It’s consolation; it’s an apology, a rubber stamp. It’s a get-out-of-jail-free card – ‘if you pass the CRA we won’t mess with you.’ When you start talking about the CRA, you have to start there. Regardless of how many billions of dollars there’s access to, I’m less impressed with the numbers. We need to be clear about its function.<sup>132</sup>

Connelly explains how the issues of community reinvestment, wealth building, and broader system change

131 “Community Reinvestment Act Performance Evaluation: National Cooperative Bank, N.A.” Office of the Comptroller of the Currency. August 8, 2016. <https://www.occ.gov/static/cra/craeval/jun17/25093.pdf>

132 Interview with Me’Lea Connelly

is more than just about addressing financial marginalization and exploitation, but rather overcoming fatal stigmas and economic barriers, particularly for the Black community.

“The reality is people are starting to correlate the economy, money, and capitalism with Black people being killed,” she observes. “They need capital and access to capital. They need homeownership and stable housing. They’re getting pulled over because they can’t afford new vehicles. Philando Castile had been pulled over 50 times, and he was pulled over [the night he was fatally shot by a police officer] with a broken tail light.”<sup>133</sup>

### **Despite the growing acceptance of the community wealth building framework and the opportunities within the CRA to utilize such approaches, the system-changing potential of the CRA is going underutilized.**

It was this understanding among community members in Minneapolis, she explains, that led to the idea of organizing a Black-led credit union, called Village Trust Financial Cooperative, in the wake of the killing of Castile. Following the shooting, the Association of Black Economic Power organized a meeting as a way to bring community members together in the wake of this tragic event. Connelly recalls that at the meeting “we ripped it up and were writing out ideas—people were talking about where do we need to invest and divest. The number one idea that came out of that meeting was a Black-led credit union in North Minneapolis.”<sup>134</sup>

133 Ibid

134 Ibid

The new credit union set to be based in North Minneapolis—a historically Black neighborhood and the site of the police shooting of Jamar Clark in 2015—is more than just about meeting the financing needs of the community. “Of course there are tons of predatory lenders charging high rates to our most vulnerable members of the community, and of course there are no other banks in the area and there’s a need for entrepreneurship because people can’t get jobs because they have records or because they’re Black—that itself is enough,” she says.<sup>135</sup>

But simply addressing financing needs is not enough to break through the systemic barriers facing the Black community. “We need to have that and create our own,” Connelly maintains. “We need to own the resources, and stop expecting that nonprofits, banks,

**“We need to own the resources, and stop expecting that nonprofits, banks, and the government are going to do it for us. They’re going to fail and exploit us in the process of doing it.”**

and the government are going to do it for us. They’re going to fail and exploit us in the process of doing it. It’s about understanding the crux and core of where injustice lies. Its home is the heart of capitalism, not the criminal justice system.”<sup>136</sup>

The development of the credit union mirrors a nationwide movement, in part led by the Blackout Coalition, to encourage the development of Black-owned and led businesses and banks. Though the credit union is a demonstration of how the traditional banks continue to fall short in addressing the legacy of redlining and break through systemic barriers in local communities Connelly, among others, still see the CRA as a tool for building the next system, alongside the ef-

135 Ibid  
136 Ibid

forts of communities looking to solutions outside the system. “As for proposals about increasing money or fixing the CRA—sure. The reparations argument has a strong argument for that,” she comments. “We have the data; we just don’t have the inertia.”<sup>137</sup>

Mark Pinsky adds that the CRA remains “important as a symbol of corporate social responsibility...There’s no CRA for consumer products,” he notes. “There is corporate social responsibility and ESG [environment, social, governance] standards, but [the CRA] is a unique law and to lose it would be a disaster.”<sup>138</sup> He adds, “the CRA should be a mechanism by which banks better serve low income communities, communities of color and women or small businesses. If you could just get the CRA refocused on actually serving the purpose it was supposed to serve, you would do massive amounts of good.”<sup>139</sup>

The key to turning the CRA into an effective tool that better embodies community wealth building approaches that facilitate systemic change lies in a point that Connelly consistently returns to. “What I always say is the only way out is through; the only way out of capitalism is through capitalism.” She explains, “What if we play the same game [of wealth accumulation] but we decide to put [the money] into a cooperative that doesn’t spend any money [in the capitalist system]. So, we change the end goal recipient.”<sup>140</sup>

April De Simone echoes this point, arguing that “the CRA is a valuable tool that just needs to be reprogrammed or tweaked to support longer-term projects that aren’t topical solutions with hidden agendas, to use it to say, ‘Hey, this is how we can continue what we want to see in our communities in a positive way, without creating another issue somewhere else.’”<sup>141</sup>

Connelly concludes:

The focus should be on our strategy of how we use this money. Not, ‘we need a fairer capital-

137 Ibid  
138 Interview with Mark Pinsky  
139 Ibid.  
140 Interview with Me’Lea Connelly  
141 Interview with April de Simone

ism'... I don't want to take away from the leaders that have to fight for the CRA, for reinvesting in communities that banks are extracting from. But that's the brilliance of capitalism; [the corporations and banks] make you fight them on something that's going to benefit them anyways.<sup>142</sup>

So, she says, "we should still fight to make sure this program is what it's supposed to be and keep the pressure up, but we should have twice that energy on a long-term strategy of how to flip that money, because right now, we've got a lot of holes in the bucket."<sup>143</sup>

As part of that strategy, she notes that the challenge is in laying the groundwork, particularly in the communities traditionally marginalized by the present system. That is, the other half of CRA reform comes with "creating a system to put people in better positions to interact with the CRA."<sup>144</sup> This involves developing the infrastructure, simplifying the logic and process, cultivating leadership and changing behavior and culture on the ground to put CRA capital towards community wealth building initiatives that help plant the seeds of system change. It is to this, and CRA reforms that would support such investments, that this working paper now turns its attention.

### Rethinking the CRA as a community wealth building tool

Richard Marsico, in his book *Democratizing Capital*, argues that "the CRA has helped to democratize capital by giving more people a voice in bank lending decisions and including more people in the economic mainstream by influencing banks to make more loans to buy homes or open small businesses."<sup>145</sup> While this may certainly be true, particularly when compared to the counterfactual of the CRA not existing in the first place, the current CRA regulatory framework—the lending, investing and services criteria, the role of the exams and examiners, and the enforcement mecha-

nisms—is not fully realizing the purported overall democratizing benefit of the CRA and could be improved in a variety of ways, including:

- The types of loans, investments and services that are encouraged (via the Interagency Q&As) currently do not include, let alone emphasize, community wealth building approaches that are increasingly becoming understood as a new generation of community development best practices. They also do not currently emphasize lending and investment to women and people of color. These could be incorporated into the Q&As either as part of a list of criteria or, more fundamentally, an expansion or revision of the definition of community development.
- The role of the agencies could be strengthened to more consistently and rigorously facilitate a greater amount of community input (such as through the Investment Connection events at the Federal Reserve District Bank of Kansas City) and to help bring greater awareness of the new generation of community development best practices to examiners, banks, community groups, and fellow regulators.
- Standardized performance contexts (i.e. the part of the exam putting community needs into context with banks' performance) could further streamline such coordination and understanding by collecting the data and knowledge held at agencies, along with community input, to be used as a more standardized assessment of bank performance (versus examiners independently writing a new performance context for each exam).
- The overall transparency of the law—e.g. its accessibility to the public—and the avenues for engagement could be strengthened by improving the accessibility of information on agency websites as well as providing finer-grained data collection (i.e. the type and ownership structure of such loans and investments).

142 Interview with Me'Lea Connelly.

143 Ibid.

144 Ibid.

145 Marsico, Richard. "Democratizing Capital: The History, Law, and Reform of the Community Reinvestment Act." *New York Law School Law Review*. Vol. 49. March 14, 2005.

- Ultimately, the expansion of the CRA beyond non-bank and non-depository institutions and the addition of new assessment areas to capture geographical areas with considerable amounts of bank lending through non-branch means is critical given that financial activity, including previously CRA-covered activity, provided outside of CRA covered institutions has expanded greatly in the last several decades.
- Improving enforcement mechanisms by increasing the range of CRA ratings and instituting greater penalties for failed CRA ratings could induce greater responsiveness to CRA criteria. Such penalties could range from the submission of improvement plans with failed CRA ratings, to financial penalties, to at the most extreme, divestment or restructuring in the form of full or partial conversion into publicly held assets.

To be clear, the commonly advocated CRA reforms mentioned at the end of Part 1 would go far in closing many of the gaps in the regulatory framework today. Indeed, several of the improvements proposed here are part of that list (such as specifying lending to communities of color and women, the standardized performance contexts, various forms of heightened transparency, and expansion of the CRA). However, what this working paper primarily seeks to add to the conversation is an emphasis on incorporating a greater focus on more equitable and inclusive economic development approaches, such as community wealth building, in the CRA-qualifying criteria and definition (in addition to data collection), as well as increasing the role of the regulatory agencies in facilitating engagement and understanding among communities, banks and examiners, and the rigor of enforcement mechanisms.

The opportunities to reform the CRA according to these proposals exist at multiple levels, from changes to the specific criteria (via the Q&As), to the changes within or among the agencies, to changes to the statutory language itself (via new legislation introduced in

Congress). The avenues through which such reforms may be advocated or proposed can be different—i.e. through comments on bank exams or merger proposals (on the agency websites) or in comments to bank examiners, to the agencies directly (from their district offices up through the FFIEC), or to members of Congress (or campaigning congressional candidates).

However, pursuing the avenues outside of the congressional route is made particularly difficult by the lack of transparency (e.g. inaccessibility of agency websites and a more general lack of transparency around how regulators take into account feedback either on exams or merger proposals) and the fact that a primary channel for public input on the CRA is through agency “notices of proposed rulemaking” or irregularly scheduled hearings on the Q&As or the CRA as a whole.

Other than community organizations issuing letters to agencies or requesting to meet with agency staff, there are very limited formal and coordinated ways to provide input to the agencies, and even within the formal avenues that dialogue is restricted. As Ellen Seidman, former director of the Office of Thrift Supervision, comments, “the problem is that there are strict rules once a [notice of proposed rulemaking] is out for how people outside the agency can communicate with the agency. So, having free-flowing dialogue is very difficult.”<sup>146</sup> Plus, there appears to be no formal way to initiate agencies issuing a notice of proposed rulemaking. This makes the National Community Reinvestment Coalition—a member-based organization—a valuable resource and avenue through which reforms may be advocated going forward, given its policy expertise and ability to channel communications with banks and community groups to regulators.

In the near term, the most recent notice of proposed rulemaking issued by the OCC (which followed the Department of the Treasury’s review of the CRA—the “Community Reinvestment Modernization Act Recommendations”)<sup>147</sup> offers a more immediate op-

<sup>146</sup> Interview with Ellen Seidman

<sup>147</sup> “Memorandum for the Office of the Comptroller of the Cur-

portunity for input to the agencies. The recommendations in the Treasury’s memorandum included some more fundamental reforms, such as redefining the assessment areas, improving the performance contexts by coordinating among federal agencies, and providing a more transparent CRA exam schedule.<sup>148</sup>

The Notice of Proposed Rulemaking issued by the OCC has followed up by requesting comments on changes related to bank ratings, redefining “community development,” adding criteria for what qualifies as CRA activity, performance contexts, redefinition of assessment areas, and data reporting. (Comments were set to be due on November 19, 2018). However, more fundamental reforms— such as expanding the CRA beyond deposit-taking institutions and instituting stricter enforcement mechanisms— will require legislative change (discussed later in this paper). This is a result of the fact that the public charter logic at the root of the CRA—that because banks receive a public benefit in the form of FDIC insurance they must serve a public benefit to the entirety of the communities they operate in—is explicitly stated in the statutory language.

While in the near-term this notice of proposed rulemaking offers an opportunity to provide comments on important reforms, the broader administrative and legal barriers demonstrate that an act of Congress is likely the most substantial (and arguably necessary) way to implement holistic and sustainable CRA reform. While reforms strengthening the CRA implemented outside the legislative process would make the CRA a better tool for community reinvestment, for the CRA to reach its fullest potential, the CRA needs to be expanded. Such an act will require legislative action, and likely some additional groundwork in developing a robust legal argument for doing so.

Secondly, if capital is to be directed towards com-

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rency, the Board of Governors of the Federal Reserve System, the Federal Deposit Insurance Corporation.” U.S. Department of Treasury. April 3, 2018. <https://home.treasury.gov/sites/default/files/2018-04/4-3-18%20CRA%20memo.pdf>

148 “NCRC Analysis of CRA Treasury report.” National Community Reinvestment Coalition. April 18, 2018. <https://ncrc.org/ncrc-analysis-of-cra-treasury-report/>

munity wealth building approaches, there needs to be investment in capacity building and groundwork. If community wealth building approaches are emphasized as part of CRA reform, the willingness and likelihood of banks to actually engage with such approaches rather than traditional practices depends in part on further building up the awareness and knowledge of such approaches (as well as further engagement by the agencies’ community development divisions). Similarly, more work needs to be done to further foster these approaches within low-income communities and communities of color (discussed more in Part 3).

**The opportunities to reform the CRA exist at multiple levels, from changes to the specific criteria (via the Q&As) and to processes within or among the agencies to changes to the statutory language itself (via new Congressional legislation).**

CRA reform will be a continual and ongoing process. More fundamental reforms may be more possible when there is more political momentum (such as achieving a Democratic majority in Congress or following another financial or economic crisis).

Moreover, CRA reform should be seen as just one part of a next system of community reinvestment. Wholesale reforms to the CRA face significant barriers; meanwhile, there are complimentary laws that equally need reinforcement as well as alternative financial institutions geared towards community reinvestment that may be pursued outside of the CRA on a more local level. Both are considered in more detail in the concluding section of this part and the policy agenda.

## Potential reforms: challenges and opportunities

### *Adding community wealth building approaches to Q&As*

Community wealth building models and approaches could be added to the Q&As in a variety of ways:

- Add criteria that specifically call for supporting minority-owned and women-owned small businesses, as well as minority- and women-focused mortgage lending.<sup>149</sup>
- Add criteria that specifically call for supporting locally owned small businesses over national corporations and franchises (determined by incorporation structure and location of owner[s] in relation to the business).
- Add specific examples of community wealth building activities to the Q&As under what qualifies as community development loans and investments, such as co-ops, worker owned businesses, ESOP companies, anchor institutions, social enterprises linked to nonprofits and community corporations, and land trusts.
- Specifically call for collaboration with community members on development projects as a component of what qualifies as community development loans, investments, and services.
- Add criteria encouraging lending and investing to more delivery channels, including government and cooperative loan funds (CDFI or non-CDFI).<sup>150</sup>
- Expand the definition of community development in the Q&As from “activities that promote economic development” through financing small businesses and mortgages to include

149 Taylor, John and Silver, Josh. “The CRA: 30 Years of Wealth Building and What We Must Do To Finish the Job.” Chapter in *Revisiting the CRA: Perspectives on the future of the Community Reinvestment Act*. Federal Reserve Banks of Boston and San Francisco. February 2009.

150 Pinsky, Mark. “CRA 2.0: Communities 2.0”. Chapter in *Revisiting the CRA: Perspectives on the future of the Community Reinvestment Act*. Federal Reserve Banks of Boston and San Francisco. February 2009.

language to the effect of “activities that promote economic development; equitable, local, and collective ownership of assets; and cross-sector community collaboration by financing models and facilitating initiatives that meet these ends” within LMI communities.

The additional criteria and changes to the community development definition could be advocated for through the process of drafting the Interagency Q&As. Revising the definition may prove to be more difficult than adding criteria. Though the agencies’ district offices (such as the separate Federal Reserve district banks) are able to operate and perform research at their divisions separately, they ultimately take their direction from federal mandate (such as from the Federal Reserve Board of Governors) and the Q&As as they are written by the federal agencies. Therefore, revision of the definition or criteria would need to occur at the federal level and be coordinated across agencies.

Even with these changes, however, barriers to adoption remain. Banks’ engagement with some of those approaches is made difficult by a general lack of expertise among traditional lenders with non-traditional business models. For instance, Ann Fedorchak, Director of Specialty Finance at the National Cooperative Bank (NCB) in Washington, DC, spoke to this in relation to cooperative development, noting, “It may be difficult for traditional lenders to understand the aspects of the cooperative business model with its unique structure, ownership and governance.” Ultimately, the best practices for co-op lending are housed in organizations that specialize in co-op lending. “It’s a niche industry,” says Fedorchak. “In the US, cooperatives are not a common business structure, so the organizations that specialize in co-op lending have had a long history of impact in the sector with good performance.”

Thus, building up greater awareness and understanding of such models is just as important as adding them as part of CRA qualifying criteria. The Democracy Collaborative’s 2016 *Strategies for Financing the In-*

*clusive Economy* report, for instance, outlines the current financing methods for financing wealth building models—to demystify the financing of broad-based enterprise—such as cooperatives, employee stock ownership plans, social enterprises, hybrid enterprise, and municipal enterprises.<sup>151</sup> Still, adding criteria that focus on cooperatively focused CDFIs (which automatically qualify given that they are certified to serve LMI communities) or CDCs may provide one way for banks to direct capital towards such models. NCB itself collaborates with a number of CDFIs to maximize its CRA efforts, particularly CDFIs that focus on co-op lending. Fedorchak adds, “We’ve had great success using this strategy. CDFIs have flexible capital that’s well suited for co-op and community development lending. It’s been a worthwhile partnership.”

However, such models also have their own unique challenges related to including low-income borrowers and communities of color. For instance, in cooperative development, member equity may present a hurdle to potential member owners. Fedorchak states, “In low-income communities, member equity and member loans may not be readily available. Fortunately, national foundations and local governments are seeing the economic benefits of cooperatives, and are starting to provide essential funding and resources.”

Ensuring efforts benefit low-income residents also remains a challenge. For example, Seward Community Co-op in Minneapolis ran into community backlash with the opening of its second store in a historically Black neighborhood.<sup>152</sup> Though the community lacked a grocery store offering fresh food options, there was concern that the store would spur gentrification in the area if the co-op did not adopt more rigorous racial equity hiring goals. Ultimately, it was the cooperative model of the business that allowed for the incorporation of this community input in the development process, resulting in even more robust ra-

151 Duncan, Violeta, Dubb, Steve, Kelly, Marjorie. “Strategies for financing the inclusive economy.” The Democracy Collaborative. September 2016.

152 Sanders-Redmond, LaDonna. “Road to Friendship: A Food Co-op in A Community of Color.” Seward Community Co-op. April 25, 2016. <http://seward.coop/posts/944>

cial equity goals for the co-op, and likely more rigorous goals than a national chain, such as Whole Foods, would have instituted.<sup>153</sup>

Another challenge arises related to classification. Given the collective ownership structure, what counts as a low-income borrower may be less clear. For instance, one interpretation is that the borrower qualifies as LMI (e.g. if the worker-owners, managers or board members are LMI). Alternatively, it could refer to whether such lending is done within an LMI census tract as is done with CDFI reporting. NCB currently categorizes its cooperative lending for CRA purposes according to LMI-qualifying census tracts or by the income level of residents in the case of affordable housing.<sup>154</sup> Limited equity co-ops are also included as low income. Lending to a cooperative business earning less than \$1 million in revenue would also automatically qualify.

### **These models have their own unique challenges related to including low-income borrowers and communities of color.**

These categorizations, however, might not be inclusive of all potential benefits to LMI borrowers. Ann Fedorchak comments that the impact cooperative businesses have on local communities does not always meet the specific parameters of the CRA regulations, and the results are not as easy to measure as with other investments, such as CDFIs. “A number of co-op loans will not qualify for CRA due to location, or they

153 Pagani, Susan. “This Cooperative Grocery Store Wants to Break the Diversity Mold.” *Civil Eats*. September 20, 2016. <http://civileats.com/2016/09/20/this-minneapolis-cooperative-grocery-store-is-working-to-break-the-diversity-mold/>

154 Email correspondence with Ann Fedorchak.

are outside of the low-income census tracts, therefore, the community benefits of the project are not reported,” notes Fedorchak. However, as a first step, categorizing such loans or investments to collectively owned businesses based on location may help guide investments towards such models.

Ultimately, simply adding community wealth building criteria to the list, or even expanding the definition of community development, will not guarantee a shift in practice. As with some of the current criteria, such as gentrification-mitigating development strategies (e.g. mixed-income housing), important criteria may be overlooked given that they are just one option among a list. Though such investments may qualify as innovative forms of lending and investing, which under the current criteria and examination procedures

**Simply adding community wealth building criteria to the list will not guarantee a shift in practice. Heightened enforcement mechanisms and expanded coverage may help.**

can help improve a banks’ scores, banks may still be less inclined to engage with such models given their unfamiliarity with them and the fact that the current enforcement mechanisms of the CRA may not sufficiently incentivize most banks to go above and beyond traditional lending and investing. This is where such changes as adding greater emphasis on the role of the agencies in facilitating collaboration among communities, examiners, and banks; adding standardized performance contexts; and instituting more enforcement mechanisms play an important role.

*Strengthening performance contexts and CRA transparency*

In addition to revisions to the Q&A criteria and

community development definition, the democratic capacity of the CRA could be improved by standardizing the performance contexts to put examiners and communities in a better position to evaluate community needs and improve the overall transparency of the CRA, such as in the following ways:

- Standardize performance contexts at the interagency level—starting with the top 100 MSAs—by utilizing data already collected by the Census Bureau and incorporating community input on the community development needs for each region. Examiners for different banks in a given region would then be pulling the same performance contexts, rather than writing their own for every single exam with mixed levels of bank and community input.<sup>155</sup>
- Account for branch closures (occurring since the bank’s prior exam) and downgrade a bank’s rating for branch closures in communities severely lacking and in need of branch access (particularly if maintaining such branches would not significantly affect bank capacity).<sup>156</sup>
- Add more transparency and rigorous scrutiny of illegal and high-cost, high risk (“predatory”) lending practices within the exams. Currently very little information is provided.<sup>157</sup>
- Ensure that exams are conducted regularly and are released in a timely way for the top 100 banks by asset size.<sup>158</sup> Require that exams be publicly announced in advance and/or list scheduled bank examinations clearly on the FFIEC website.

155 Silver, Josh. “CRA Performance Context: Why it is Important for Community Development and How to Improve It.” National Community Reinvestment Coalition. 2016.

156 “2016 Policy Agenda: Investing in a Just Economy.” National Community Reinvestment Coalition. 2016.

157 Taylor, John and Silver, Josh. “The CRA: 30 Years of Wealth Building and What We Must Do To Finish the Job.” Chapter in *Revisiting the CRA: Perspectives on the future of the Community Reinvestment Act*. Federal Reserve Banks of Boston and San Francisco. February 2009.

158 “2017 Policy Agenda: Investing in a Just Economy.” National Community Reinvestment Coalition. 2017.



- Improve data collection on the race and gender of all borrowers.<sup>159</sup>
- Improve data collection on the types of businesses and ownership structure of businesses financed.
- Improve accessibility of information on agency websites by consolidating and/or streamlining information about the CRA through the FFIEC and main Federal Reserve websites. Currently information and resources are spread across the various agencies' websites.<sup>160</sup>

The recently released Treasury memorandum includes the performance contexts as part of their policy recommendations, though whether or not they make their way into reforms still depends on their adoption by the agencies. NCRC wrote an extensive 2016 report, “CRA Performance Context: Why it is Important for Community Development and How to Improve it,” which goes into excellent detail on how performance contexts are currently conducted, why they are important, and specifics on how they could be improved. The main benefit to be highlighted here—beyond efficiencies—is that standardizing the information gathered on community needs, and ensuring this is consistent and accessible to the public, could help increase the ease and role of community input on CRA exams. Such reforms would require coordination at the interagency level.

NCRC also reports on strategies to improve transparency, outlining potential benefits through their annual policy briefs and other articles—only several of which have been included above. The Treasury memorandum has also included transparency, calling for a regular and public-facing CRA exam schedule which would further help communities engage with the evaluation process. Meanwhile, several improve-

159 Ibid.

160 “Testimony of Josh Silver, Senior Advisor, NCRC, Regarding the Regulatory Review Mandated by the Economic Growth and Regulatory Paperwork Reduction Act (EGRPRA).” EGRPRA Washington, DC Outreach Meeting conducted by FDIC, OCC, and Federal Reserve Board December 2, 2015. Testimony published by National Community Reinvestment Coalition.

ments to data collection would help provide an understanding of the types of projects and demographics the CRA is serving. For instance, NCB’s CRA exam did not distinguish between non-cooperative and cooperative projects among LMI qualifying loans and investments. Such distinctions would help provide a better assessment of the type of lending banks are actually doing beyond the bucket categories of “small business,” “community development,” or “mortgages,” which would help in understanding what of the specific criteria is getting prioritized. Reforms to data collection and transparency would also likely require coordination at the interagency level. However, each agency could independently do more to improve how accessible and up-to-date their websites are with respect to CRA information and community input.

### *Strengthening the role of the agencies*

The community development divisions at each of the agencies—the OCC, the Fed, and the FDIC (which have jurisdiction over nationally chartered, state-chartered member banks and state-chartered non-member banks respectively)—could be more consistently and rigorously leveraged as a way to close disconnects between their examination divisions and community affairs offices that are more up-to-date on community development best practices, as well as between banks. This could be achieved through strategies such as these:

- Encourage agencies to include in their research on community development best practices technical assistance manuals, case studies, or guides to local resources to support the emerging new set of community wealth building models.
- Encourage or require agencies to play an even more central and consistent role in facilitating communication between community groups, banks, and examiners. This facilitation role can be modeled on the place-based “Investment Connection” events used in recent years to connect community groups and banks in a given area around new CRA-

qualifying projects. Other similar events held on an annual basis could be geared towards building understanding of community needs (the comments of which could go towards informing the standardized performance contexts for that region), analyzing community development best practices, and collectively prioritizing points of focus for community development projects in the coming year.

- Realign the work of the examiners with that of the agencies' community development divisions. Rather than training examiners exclusively on the CRA criteria and exam procedures while the community development functions of the agencies' community affairs offices (in which all the updated knowledge on best practices and community contacts is housed) remain largely separate, communication, recruitment, and training between the two could be more integrated.

**The success of these proposals hinges primarily on the ability to change institutional behavior at the agencies at all levels, and in the case of the Federal Reserve, to align the interests of all the district banks towards performing this function.**

The proposals to leverage the agencies' community development divisions and change the role of examiners are more necessary in some communities than others, as the level of involvement currently varies across districts. If all became much more engaged with respect to the above two points, this would help close the gap between banks, communities, regulators, and the CRA language with regard to understanding both community development needs and updated community development best practices that support

non-traditional models. That is, it would position the agencies to play an instrumental role in streamlining communication among banks, community groups, and examiners.

With the agencies serving as a facilitator for this participatory dialogue, many banks may be able and inclined to learn about new community development approaches and opportunities for such investment in their communities. The Investment Connection events held by the Federal Reserve Bank of Kansas City, for instance, are focused mini-conferences to connect funders with community development projects prepared and presented by community organizations. To the extent that these conferences are expanding to more communities, and more communities and funders engage with the Investment Connection online platform, more projects entailing community wealth building approaches (such as land trusts, co-operatives, or social enterprise) may make their way to the attention of regulators and banks and build their understanding of the feasibility of such models. At the same time, the agencies' community development divisions can focus more of their research attention and resources on writing technical assistance manuals, case studies, or guides to local resources for supporting the emerging new set of community wealth building models. Such events would also be an opportunity for community groups and regulators to identify community needs, the feedback of which could then be channeled to the standardized performance contexts via the agencies.

Moreover, this approach utilizes the existing resources of the agencies in terms of their place-based regional offices, existing community relationships, and stores of economic and community development research and expertise. It further elevates the voices and expertise held in community organizers and community development practitioners by providing more equal grounds for dialogue, as opposed to banks picking and choosing what groups to work with and what projects to take on. Meanwhile, examiners could be brought more into conversation with the community development affairs offices by either offering cross-

trainings on community development best practices or by providing examination procedures that include additional guidance on innovative community development models and approaches that may receive special consideration.

However, the success of these proposals hinges primarily on the ability to change institutional behavior at the agencies at all levels, and in the case of the Federal Reserve, to align the interests of all the district banks towards performing this function. Such changes are running against the institutional inertia of decades of piece-by-piece construction of the CRA regulatory framework. Moreover, each district bank (at least in the case of the Federal Reserve) operates independently and has developed its own culture and ideology, shaped over time by its regional context and district presidents. Also, importantly, the directors of such agencies are appointed by the president (and approved by the Senate), which can set the overall tone of what range of reforms may be considered by the agencies.

Though the advent of the Investment Connection meetings is a promising sign of a willingness for, at least, some of the community development divisions at the Federal Reserve to take a more active role in facilitating dialogue around the CRA, it is not guaranteed that all of the Federal Reserve's independent district banks or the other agencies would adopt their use (due to cultural and ideological differences) or would pursue some form of integration between exam staff and the community development divisions. Likely, the only way to align the independent Federal Reserve's district banks or the district agency offices of the OCC and FDIC around a certain objective or function is through a federal mandate or initiative from the respective federal agencies.

For these mandates or initiatives to resemble one another, the agencies would need to coordinate on an interagency basis. Historically such initiatives typically come about following moments of crisis (such as during the financial crisis, when the Federal Reserve Board began a systemwide effort to coordinate with

all the district banks to do research into what was driving foreclosures).<sup>161</sup>

Alternatively, though perhaps less likely, either a separate institution could be established to perform this function (similar to the way the Dodd-Frank Act established the Consumer Financial Protection Bureau), or the community development divisions at the district banks could be spun off and put under the umbrella of a separate institution with a federal directive. That is, the existing resources with respect to community development within the agencies could be transferred to a national "community development bureau" of sorts. This could on the one hand heighten the level of coordination and reduce inefficiencies and discrepancies in CRA implementation, but it could also centralize the target of efforts to dismantle the CRA regulatory framework and related community development efforts. Regardless, of course, this would also necessarily come as a result of additional legislation.

#### *Expanding the CRA beyond depository institutions and branches*

There are several ways the CRA can be expanded beyond depository institutions and branches, such as by:

- Redefining assessment areas by market share of banking activity in addition to branch presence. This may involve extending assessment areas to communities where banks do not have branches but have significant lending activity. For banks that have smaller market shares across a wide geographic area, a region or maybe the entire country could serve as their assessment area. For certain banks, particularly where a significant amount of activity is occurring outside of the bank's branch areas, this is already being done by regulatory agencies, though not consistently and with scattered justification.<sup>162</sup>

161 "Promoting Consumer Protection and Community Development." The Federal Reserve. [https://www.federalreserve.gov/aboutthefed/files/pf\\_7.pdf](https://www.federalreserve.gov/aboutthefed/files/pf_7.pdf)

162 Olsen, John et al. "A Framework for Revisiting the CRA." Chapter in *Revisiting the CRA: Perspectives on the future of the Community Reinvestment Act*. Federal Reserve Banks of Boston and San Francisco.

The agencies may also independently instruct examiners to consider certain assessment areas as full scope (as they would with assessment areas that have bank branches).<sup>163</sup>

- Including nonbank mortgage affiliates in CRA exams. The inclusion of lending activity by mortgage lenders that are affiliates in the same bank holding company as a CRA-covered institution (that the commercial bank arm of a bank could otherwise perform) in CRA exams is currently optional. Including them would help remove the regulatory arbitrage and grade inflation caused by a significant amount of a bank's lending activity occurring in a non-CRA covered affiliate.<sup>164</sup>
- Including nonbank affiliates that perform any financial activity on CRA exams. This proposal would essentially extend the CRA to all financial institutions by covering the investment banking, insurance, credit card, and on-line banking arms of bank holding companies. Again, the logic is similar in that any activity in a given area performed by these institutions would activate CRA examination.<sup>165</sup>
- Expanding the CRA to all financial institutions, including credit unions. Rather than maneuvering the language of the current CRA to include affiliates, expansion to all financial institutions could be proposed as part of a new

bill explicitly stating CRA-like obligations for all financial institutions. The 2009 CRA Modernization Act attempted to do so, though this route could be attempted again.<sup>166</sup>

The avenues for expansion of the CRA listed above include a variety of mechanisms for the CRA to include additional financial institutions. To some extent, some of these are already being pursued by regulators. For instance, the agencies may issue guidance to examiners to review an assessment area as full scope to receive careful review, or some service areas may be included for review as result of banks performing substantial financial activity there, despite not having bank branches in that area.<sup>167</sup> However, these changes are inconsistent and more wholesale changes to how assessment areas are defined, or what institutions are covered by the CRA, will require coordination at the interagency level if not through legislative change. Seidman explains that though accomplishing some of these reforms outside of Congress and through the regulatory agencies is possible, that does not necessarily make it more politically feasible:

The question of how you define assessment areas and whether that really does have to be related to deposits, that's again one of those ambiguous ones where if you had regulators that really, really wanted to do something constructive and creative and they thought they had the wind at their backs, they could probably put together the legal case that they could do it and let the court make the decision. But it's ambiguous enough that unless they really want to do it, they would probably have to go the statutory route... [As for] how you deal with the affiliates, there are probably some clever ways to bring affiliate activities into CRA consideration, but actually bringing in other entities requires statutory change.<sup>168</sup>

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February 2009. Silver, Josh. "The Community Reinvestment Act and Geography: How Well Do CRA Exams Cover the Geographical Areas that Banks Serve?" National Community Reinvestment Coalition. April 2017.

163 Email correspondence with Josh Silver.

164 Taylor, John and Silver, Josh. "The CRA: 30 Years of Wealth Building and What We Must Do To Finish the Job." Chapter in "Revisiting the CRA: Perspectives on the future of the Community Reinvestment Act. Federal Reserve Banks of Boston and San Francisco. February 2009. Silver, Josh. "The Community Reinvestment Act and Geography: How Well Do CRA Exams Cover the Geographical Areas that Banks Serve?" National Community Reinvestment Coalition. April 2017.

165 Taylor, John and Silver, Josh. "The CRA: 30 Years of Wealth Building and What We Must Do To Finish the Job." Chapter in "Revisiting the CRA: Perspectives on the future of the Community Reinvestment Act. Federal Reserve Banks of Boston and San Francisco. February 2009.

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166 "Community Reinvestment Act of 2009." H. R. 1479. 111th Cong.

167 Email correspondence with Josh Silver.

168 Interview with Ellen Seidman

Thus, the primary challenge to expanding the CRA is the original legislative language. The language used by the original authors was to do something fairly simple—to call on banks to lend in LMI communities surrounding their bank branches. However, this original logic and statutory language of the CRA does not go far enough to assert a more fundamental obligation to require financial institutions that have expanded outside of the CRA to take a role in addressing the social and economic issues endemic to the country. The bank holding company clarification stated by the Federal Reserve Board of Governors in 1972 arguably got much closer, in asserting that “bank holding companies possess a unique combination of financial and managerial resources making them particularly suited for a meaningful and substantial role in remedying our social ills,” though there is no regulatory or enforcement mechanism outside of the CRA that acts on this assertion. Consequently, any wholesale changes will likely require legislative action.

Another challenge to expansion is establishing the legal justification for doing so. The logic often employed in the argument to extend the CRA to all financial institutions is that depository institutions receive a public benefit in the form of FDIC insurance, and thus should be held accountable. The fact that all financial institutions—including investment banks, mortgage companies, and insurance companies—are implicitly receiving government backing in the form of bank bailouts (as evidenced in the most recent financial crisis) would suggest that such institutions receive similar public backing and thus should be held to a similar level of accountability.<sup>169</sup> Though true, this argument runs counter to the intent of the Dodd-Frank Act to *remove* that implicit guarantee by ending ‘too big to fail’-induced bailouts. Thus, arguments for expanding CRA coverage to other financial institutions because they receive public backing runs the risk of further entrenching underlying concerns about the current financial system. (Note that the

169 Olsen, John et al. “A Framework for Revisiting the CRA.” Chapter in *Revisiting the CRA: Perspectives on the future of the Community Reinvestment Act*. Federal Reserve Banks of Boston and San Francisco. February 2009.

CRA Modernization Act did not explicitly use this argument in its proposed statutory language.)<sup>170</sup>

There is, however, an opportunity to expand the argument around public accountability that does not rely on government bailouts. There is implicit government support for all financial institutions outside of government bailouts—whether through upholding contracts, enforcing antitrust laws, maintaining security exchanges, providing short-term financing in the discount window, or any of the many functions the Federal Reserve plays that maintain the money supply and stabilizes growth. In that case, the logic for extending the CRA or a CRA-like law could involve

**The logic for extending the CRA or a CRA-like law could involve a much more affirmative obligation that calls out directly the nature of banks, their role in the economy, and their role in addressing social and economic issues.**

a much more affirmative obligation that calls out directly the nature of banks, their role in the economy, and their role in addressing social and economic issues (similar to the way the 1972 bank holding company revision quoted above did).

One way to potentially build out this legal justification is to further build on the notion of “public convenience and necessity” used in legislation pertaining to public service industries—i.e. private corporations that do business with the public, such as transportation, communications, power, and sanitary services. This legal concept was in part what informed the CRA in the first place, as told by organizers working closely with drafting the original legislation (see “The origin of the Community Reinvestment Act” sidebar on page 13). Under the notion of “public convenience

170 “Community Reinvestment Act of 2009.” H. R. 1479. 111th Cong.

and necessity,” companies in such industries receive their charters and permission to do business with the public conditioned on having met certain performance criteria. At the time of the CRA’s passage, it would have made sense to limit this logic to the provision of charters to banks receiving FDIC insurance, and basing the assessment area on physical bank branches. However, such logic could be applied to any financial institution dealing with the public through other channels as well (e.g. online). This is in part contingent on the degree to which certain investment banks or other investment companies are considered as “dealing with the public.” More work done by legal scholars and policymakers would help better build out this justification. Providing justification that asserts a more fundamental obligation of banks will be important to passing effective and enduring legislation.

**The OCC’s most recent Notice of Proposed Rulemaking requests comments on introducing a “metric-based performance measurement system.” Such a system could severely lessen the importance of a banks’ responsiveness to the needs of their assessment areas.**

Still, passing such a bill through Congress is yet another matter, and would likely require some form of political momentum (such as building off of a moment of crisis). And even if legislation expanding the CRA to *all* financial institutions were to pass through Congress, it may still get held up in court over questions of legal justification. Focusing in on expansion of the CRA to mortgage affiliates, online financial institutions providing similar services to CRA-covered institutions, and credit unions (along with changes to

the assessment areas) could help lower the risk of a judicial challenge. Technically speaking, an executive order could be introduced to spur momentum, but it too runs the risk of facing the same legal challenges.

*Improving enforcement mechanisms*

Currently, the main enforcement mechanism of the CRA is that poor CRA ratings are taken into consideration in banks’ applications for a national charter, bank branches, and mergers and acquisitions. Newly chartered state banks may also be denied deposit insurance in light of poor CRA ratings. Given that many of the largest banks are already national in scope and have gone through extensive consolidation (the top 10 of which hold over 50 percent of the banking industry’s assets),<sup>171</sup> how adequate an incentive these enforcement mechanisms are is not clear. Moreover, 89 percent of banks examined in 2014 received a rating of “satisfactory,” which suggests the incentives to receive an “outstanding” rating are lacking. Banks receiving an overall performance of “satisfactory” may have performed poorly in certain assessment areas or a certain part of the exam, and the overall rating can obscure accountability for improvement in specific areas. Even if a bank receives a less than satisfactory rating, applications for mergers and expansions may be considered on a case-by-case basis and a poor rating does not result in automatic denial or plans for improvement. There are also not clear mechanisms to understand the public benefits of a merger regardless of the bank’s CRA rating.

The OCC’s most recent Notice of Proposed Rulemaking requests comments on reforming this rating system by introducing a “metric-based performance measurement system with thresholds or ranges (benchmarks) that correspond to the four statutory CRA rating categories.”<sup>172</sup> This could involve, for example, introducing benchmarks for the dollar amount

171 Calculated from the “Federal Reserve Statistical Release: Large Commercial Banks.” The Federal Reserve. June 30, 2018. <https://www.federalreserve.gov/releases/lbr/current/>

172 *Reforming the Community Reinvestment Act Regulatory Framework.* Department of the Treasury, Office of the Comptroller of the Currency. August 28, 2018, p. 15. <https://www.occ.gov/news-issuances/bulletins/2018/bulletin-2018-24.html>

of CRA-related activity as a percent of total bank assets required to achieve certain ratings. The OCC writes in its notice that such a metric-based system could allow for greater flexibility, transparency, and certainty around performance ratings. This could potentially provide clarity on what constitutes a “Needs to Improve” vs. a “Satisfactory” or “Outstanding” performance and in turn mitigate the issue of rating inflation that emerges in part to lack of clarity of what exactly constitutes a “satisfactory” rating.

However, as NCRC cautions, such a ratio or a similar systematized metric-based system would severely lessen the importance of assessing banks’ performance based on their responsiveness to the needs of their assessment areas as well as community input.<sup>173</sup> That is, reducing performance evaluation to just one number reflecting the basic quantity of lending does not evaluate a bank based on its responsiveness to its assessment areas—the core intent of the CRA.<sup>174</sup> Moreover, it arguably disincentivizes higher impact but potentially more complicated or costly projects—such as loans to non-traditional business types or providing grants or patient capital—given that it would seem to incentivize big-dollar projects. This would arguably further inflate the degree to which the bank ratings do not reflect the extent to which they are serving their assessment areas. Moreover, there still remains the issue that there is no incentive for a bank to improve its performance from “satisfactory” to “outstanding” or serious disincentive to slip from “outstanding” to merely “satisfactory,” and thus enforcement issues would still remain with a metric-based system.

Thus, outside of this proposed reform, opportunities to improve the enforcement mechanisms exist at several levels, ranging from improvements within the current CRA framework, primarily around how merger applications are considered, to adding more punitive mechanisms via legislative change:

- Provide a template for banks to outline the public benefits of a proposed merger.<sup>175</sup>
- Hold more public hearings on merger applications and incorporate more conditions into contentious merger approvals.<sup>176</sup>
- Require regulatory enforcement and the submission of improvement plans for any assessment area receiving a low score due to poor or fair lending performance.<sup>177</sup>
- Increase the number of possible ratings to address grade inflation by creating incentives for differentiation and the ability to discern among “satisfactory” ratings.<sup>178</sup>
- Institute a financial penalty for poor CRA ratings.
- Institute a penalty for poor CRA ratings in the form of divestment or restructuring in the form of full or partial conversion into publicly held assets or the transfer of assets to an institution with a more explicit orientation towards community investment.

All but the final two recommendations listed above could be achieved within the current CRA regulatory framework. The recommendations pertaining to proposed mergers and public input on merger applications, as well as requiring the submission of improvement plans for poor performance in certain assessment areas, will require action on the part of the regulatory agencies either independently or in coordination with one another. Changes to the ratings scale to differentiate among “satisfactory” ratings will likely require coordination among the regulatory agencies and the provision of new examination procedures.

173 Silver, Josh. “The One Big CRA Fight Over the One Ratio.” National Community Reinvestment Coalition. August 21, 2018. <https://ncrc.org/the-one-big-cra-fight-over-the-one-ratio/>  
174 Ibid.

175 “2016 Policy Agenda: Investing in a Just Economy.” National Community Reinvestment Coalition. 2016.  
176 Taylor, John and Silver, Josh. “The CRA: 30 Years of Wealth Building and What We Must Do To Finish the Job.” Chapter in *Revisiting the CRA: Perspectives on the future of the Community Reinvestment Act*. Federal Reserve Banks of Boston and San Francisco. February 2009.  
177 Ibid.  
178 Ibid.

The final two recommendations would need to be written into new legislation. Instituting a financial penalty for poor CRA ratings would be more akin to financial penalties banks face if they violate, for instance, the Sherman Antitrust Act. Such penalties are enforced by the financial regulatory agencies and the Justice Department. These fines could go towards the agencies themselves; mandated to go towards community investment programs, such as the CDFI fund; or support the establishment of a public bank (i.e. a government-owned bank, like the Bank of North Dakota) or a publicly funded cooperative development or community-focused lending institution. For instance, the NCB was founded in 1978 with \$184 million in “seed money” that Congress appropriated and after being privatized in 1981 has since grown to an asset size of \$2.3 billion.<sup>179</sup> Moreover, penalizing banks via fees is not unprecedented. In the 10 years since the financial crisis, banks have paid over \$321 billion in fines primarily to regulators, the Justice Department, the U.S. Department of Housing and Urban Development, and the Federal Housing Finance Agency.<sup>180</sup>

The more severe penalty proposed entails that actual assets of banks with a poor CRA ratings—not just fines—could be divested or otherwise restructured (in full or in part) as a public bank, a cooperatively owned or cooperative-focused bank, or a bank with an express mission for financing community development. This, in effect, already happens when a bank fails and the FDIC takes it over (quite efficiently, as it turns out) until another, usually larger, bank purchases it.<sup>181</sup> The key difference would be that the underlying model of the bank would be fundamentally changed in response to a banks’ poor performance on the CRA, as opposed to being incorporated into an

even larger bank with effectively the same model as the one that failed.

These reforms, though more extreme than what has been considered thus far, would be a more systemic approach to CRA enforcement, and particularly impactful if paired with other changes to the CRA such as the inclusion of community wealth building approaches, increasing involvement of regulators, and expanding coverage of the CRA. If properly enforced, these reforms could further direct more assets towards publicly or collectively owned financial institutions or institutions dedicated to cooperative or community development—such as National Cooperative Bank, or a community development bank or bank holding company (e.g. the Shorebank model discussed by Ron Grzywinski in the CRA origin sidebar in Part 1). Collectively owned financial institutions may include credit unions, which are for-profit institutions that function just like traditional banks, but are “specifically created to work in markets underserved by traditional capital” (regardless of whether they are registered CDFIs) and are cooperatively owned by their members.<sup>182</sup>

Public banks on the other hand could be established independently or as a part of restructuring banks with failed CRA ratings. Public, or government-owned banks, are banks owned by a public entity (either city, state, or national government) with a mandate that “begins with the public’s interest.”<sup>183</sup> They can be depository institutions or non-depository institutions with a mission focused on certain social and economic investments. With the bank being owned by the government, the profits can then be returned to the general fund of that public entity (as is the case with the Bank of North Dakota, currently the only public bank in the U.S.), which can help lower the tax burden and lower interest rates on public projects. They can also be directed to fund specific social services or forms of economic development. For instance, the Business

179 “History of Community Impact.” National Cooperative Bank. 2016. <https://ncb.coop/ncb/about-ncb/community-impact#1970s>. “Annual Report 2016.” National Cooperative Bank. 2016. <https://ncb.coop/ArticleDocuments/250/NCB%20Annual%20Report%202016FinalWeb.pdf.aspx>

180 Cox, Jeff. “Banks have paid \$321 billion in fines since the crisis (but they’ve made almost \$1 trillion).” *CNBC*. March 3, 2017. Schoen, John W. “7 years on from crisis, \$150 billion in bank fines and penalties.” *CNBC*. April 30, 2015.

181 Joffe-Walt, Chana. “Anatomy of a Bank Takeover.” *National Public Radio*. March 26, 2009.

182 *Community Development Investment Review*. Federal Reserve Bank of San Francisco. Vol 6 (1). 2010.

183 “Introduction to Public Banking.” Public Banking Institute. 2017. [http://www.publicbankinginstitute.org/intro\\_to\\_public\\_banking](http://www.publicbankinginstitute.org/intro_to_public_banking)



Development Bank of Canada focuses on small-to-medium enterprise entrepreneurial lending.<sup>184</sup> Other industrialized countries make more robust use of public banks. As of 2011, Germany's 39 public banks held 24 percent of the banking industry market share and Switzerland's 19 public banks held a 23 percent market share.<sup>185</sup>

Within the United States, public banks have increasingly made their way onto the agendas of campaigning policymakers at the local and state level, and more research is being conducted to develop best practices for preventing mission drift.<sup>186</sup> A further opportunity to establish public banks at the national level would be following a financial crisis. Several governments—such as Iceland and the UK<sup>187</sup>—nationalized some of their largest banks following the 2008 crisis rather than bailing them out using taxpayer money (such as the \$700 billion Troubled Assets Relief Program used in the U.S.). Such nationalizations can involve the government acquiring a total or controlling share of the banks' assets, which can be used to monitor or alter the banks' operations.

While public banks or other community-focused financial institutions could be pursued independently, within the CRA, more stringent enforcement mechanisms penalizing traditional banks for failed CRA exams would require legislative change and thus congressional approval, which would likely not be any less difficult than efforts to expand the CRA to other financial institutions. There are in addition certain risks of attempting to institute such penalties. A primary one would be, given that a significant amount

of financial activity by investment banks involves securities trading (much of which has an incredibly ambiguous public purpose), requiring such institutions to have a fundamental public purpose could push more of their current financial activity further into the “shadow banking system,” a network of institutions that deal directly with one another outside of regulated clearing mechanisms that provide transparency and accountability in the financial system.<sup>188</sup> It is estimated that a quarter of all global financial activity currently occurs in the shadow banking system, which includes institutions such as hedge funds. These institutions are responsible for the highest income gains for the top 1 percent).<sup>189</sup> Pairing such penalties with the Federal Reserve of Minneapolis' proposed tax on shadow banking institutions as part of their “Minneapolis Plan to End Too Big To Fail” might help mitigate this.<sup>190</sup>

### **More stringent enforcement mechanisms penalizing traditional banks for failed CRA exams would require congressional approval, as would expanding the CRA to other financial institutions.**

Another risk of instituting such penalties that may or may not factor into policymakers' reasoning is the risk capital flight (capital rapidly leaving the country). However, the extent to which capital flight is a fatal threat in the U.S. context is arguably unclear—

184 “Case Study: Business Development Bank of Canada.” Centre for Public Impact. March 27, 2017. <https://www.centreforpublicimpact.org/case-study/business-development-bank-canada/>

185 Schmit, Mathias et al. “Public Financial Institutions in Europe.” European Association of Public Banks AISBL. March 2011. P. 53.

186 Morton, Heather. “Many States see the Potential of Public Banking.” *The New York Times*. October 1, 2013. Scherrer, Christoph. “Keeping public banks accountable to the public” Part V of *Public Banks in the Age of Financialization: A Comparative Perspective*. (Edward Elgar Publishing Inc. 2017).

187 “How did Iceland clean up its banks?” The BBC. February 10, 2016. <https://www.bbc.com/news/business-35485876>. Demetriades, et al. “There should be no rush to privatise government owned banks.” *VOX CEPR Policy Portal*. January 20, 2010. <https://voxeu.org/article/don-t-rush-privatise-government-owned-banks>

188 “Shadow Banking Around the Globe: How Large, and How Risky?” from *The Global Financial Stability Report: Risk Taking, Liquidity, and Shadow Banking – Curbing Excess While Promoting Growth*. International Monetary Fund. October 2014, 68.

189 Ibid. Krugman, Paul. “Why We're in a New Gilded Age.” *The New York Review of Books*. May 8, 2014.

190 *The Minneapolis Plan to End Too Big to Fail: Summary for Policymakers*. Minneapolis Federal Reserve District Bank. 2018. <https://minneapolisfed.org/publications/special-studies/endingtbtf/final-proposal/summary-for-policymakers>

the economic strength of the U.S. globally (at least for now) and the perceived security of its assets above all others is such that international investors may be more tolerant of such a structural transition. This is partly evidenced in the fact that, following the most recent financial crisis, the U.S. experienced net inflows of capital despite that the crisis itself originated in U.S. financial institutions.<sup>191</sup>

## CRA reform: One piece of the next system puzzle

In order to optimize the CRA as a tool for building community wealth, holistic CRA reform would include reforms across all of these intervention points: encouraging community wealth building approaches, strengthening enforcement mechanisms, and expanding the scope of institutions covered by the CRA. Additions to the Q&As to include more community wealth building approaches and to expand the definition of community reinvestment to consider “economic development” as activities that build equitably, locally, and promote collective or public ownership would bring attention to those approaches that seek to democratize and stabilize assets at the local level. Regulatory agencies can better connect banks with such community development projects and examiners to advance these community development best practices.

Ultimately, though, without stricter enforcement mechanisms, banks may not have the incentive to go above and beyond to engage with communities or with such approaches even with this infrastructure. And while any amount of reform would make the CRA a better tool for community reinvestment, expanding coverage remains the most fundamental to make the CRA a core part of the country’s system of community reinvestment. “The CRA really has done a lot of good, but a lot of times there are abuses outside of CRA,” comments Josh Silver of NCRC. “It hasn’t been updated enough to keep pace with finan-

cial industry, and what is now the Wild West of the financial industry is not CRA covered.”<sup>192</sup>

The OCC’s recently issued “notice of proposed rule-making” is an opportunity in the short term to advocate for many of these reforms. Whether or not they may be included in this notice or in future notices remains to be seen. Moreover, though many of the reforms mentioned above can be implemented through the existing CRA regulatory framework via the agencies, more fundamental and holistic reforms (including expansion of the CRA and penalties for poor performance) would ultimately require an act of Congress.

The policy agenda in the next section outlines the reforms most pertinent to making the CRA a tool for community wealth, the key regulatory body involved, and suggestions for how advocacy efforts may be directed as political opportunities present themselves in the coming years. Though geared towards 2020—assuming that the more fundamental reforms will not be addressed through the agencies or considered in the current Congress—such reforms remain pertinent for any time the political momentum and energy is right to consider such reforms (such as following a moment of crisis).

Regardless of what reforms may or may not come to fruition, the CRA ultimately needs to be considered as part of a broader framework, or system, of community reinvestment. For one, there are several accompanying regulations and agencies related to community investment that must remain in place and be strengthened, such as the Federal Housing Authority, Fannie Mae and Freddie Mac, the National Housing Trust Fund, Capital Magnet Fund, the Department of Housing and Urban Development, the Consumer Financial Protection Bureau, and the Dodd-Frank Act. NCRC regularly reviews improvements to the processes and policies of such agencies in their annual policy agendas. Dodd-Frank, in particular, remains important legislation to protect as it addresses many of the practices (such as lending to unqualified bor-

191 Oatley, Thomas, Winecoff, W. Kindred, Pennock, Andrew and Danzman, Sarah. “The Political Economy of Global Finance: A Network Model.” *Perspectives on Politics*, Vol 11(1). March 2013, 113-153.

192 Interview with Josh Silver.

rowers) and other systemic issues that in part led to the 2008 financial crisis.

Even as too-big-to-fail financial institutions remain an issue, the current administration continually threatens to weaken Dodd-Frank. Congress already took action to change the asset size of banks subject to many of Dodd-Frank's provisions from \$50 billion to \$250 billion, reducing the number of banks it applies to from 38 to 12. The Federal Reserve has also proposed measures to weaken the Volcker Rule<sup>193</sup>—which put limits on the ability for commercial banks to engage in security trading (thereby putting deposits at risk. Further efforts to weaken the rule may be sought by Republican leaders in Congress.<sup>194</sup>

Outside of defending and bolstering existing legislation, other financing strategies and institutions for community wealth building need to continue to be cultivated and developed. Many of these strategies and institutions that could be part of a next system of community reinvestment are outlined in The Democracy Collaborative's 2016 Strategies for *Financing the Inclusive Economy* report.

These strategies and institutions can be strengthened alongside CRA reform, a strategic necessity given the structural and ideological barriers to sweeping CRA reform. Such institutions include government-owned banks, community and cooperatively focused credit unions, or other community development banks with an expressed mission to focus on community or cooperative investment. Public banks can be advocated for both locally—at the city or state level—and nationally, while community development or cooperative banks can be developed by community organizers, such as in case of the Village Trust Financial Cooperative of North Minneapolis (discussed in “The Community Wealth building Approach, System Change and The CRA”).

193 Cheng, Evelyn. “The Fed just proposed a plan to make life easier for banks by loosening the ‘Volcker Rule.’” *CNBC*. May 30, 2018.

194 Yglesias, Matthew. “Republicans are sowing the seeds of the next financial crisis: It's way bigger than the Volcker Rule.” *Vox*. May 31, 2018.

Meanwhile, while the focus on the CRA should remain on low- and moderate-income communities, community wealth building models ought to continue to be expanded even if they are not considered low-income qualifying for the purposes of the CRA. Fedorchak notes, “There are many benefits and services that cooperatives provide to their communities—they create jobs, build wealth and stabilize transitioning neighborhoods. On the surface, there are co-op loans that may not fit the regulatory requirements for CRA, but these transactions should not be overlooked or discredited.”

**Regardless of what reforms may or may not come to fruition, the CRA ultimately needs to be considered as part of a broader framework, or system, of community reinvestment.**

Communities across the country continue to build up these approaches, and in particular put lower-income communities in a better position to be part of the development of such approaches, as highlighted in The Democracy Collaborative's *Cities Building Community Wealth* report, among others.

Ultimately, the policy agenda outlined in the final part views the CRA as just one piece of the puzzle to bringing about a next system of community reinvestment—one that extends the CRA to a broader portion of the financial industry while also helping to plant the seeds of system change by investing in community wealth building models, which includes supporting regulations and financial institutions that promote the security and equitability of such community reinvestment.

## Part 3: A policy agenda for community reinvestment

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### Advocacy routes for a next system of community reinvestment

The following policy agenda proposes holistic Community Reinvestment Act reform, including the Act's general expansion and the addition of enforcement mechanisms to strengthen the CRA's impact as a catalyst for community wealth building. Without such expansion and enforcement, the CRA is likely to remain a tool of limited influence in an ever-expanding financial industry, allowing banks to ignore even the most minor reforms. In addition to broad reform to the CRA itself, the law must be supported by accompanying regulations and the development of institutions that ensure that the structural changes to the law occur within a supportive ecosystem that helps solidify a next system of community investment.

First, it is worth noting that the working paper thus far has highlighted significant challenges to sweeping reform, including the fact that the language of the original Act pertained to depository institutions and relied on a legal justification of community investment based in the public charter status of deposit-taking banks. Expansion of the law would thus require legislative change, and as the paper has highlighted, structural and ideological barriers exist to passing such legislation. Therefore, the policy points should neither be seen as necessarily collectively exhaustive, nor necessarily specific to being achieved in

2020, but rather as containing the core objectives that may be limited or expanded upon depending on what political opportunities become available. The CRA modernization bill introduced by Senator Elizabeth Warren earlier in 2017 offers one opportunity to organize and advocate for policy proposals in line with those proposed in this chapter.<sup>195</sup>

Similarly, in the face of uncertainty of how exactly political developments will proceed, the strategy for advocating CRA policy reforms ought to be on all fronts to keep all options available. For instance, the Office of the Comptroller of the Currency (OCC) recently issued a Notice of Proposed Rulemaking, which requests comments on reforms related to redefining community development and adding criteria for what qualifies as CRA activity, performance contexts, redefinition of assessment areas, and data reporting. (Comments were set to be due on November 19, 2018.)

Given the uncertainty of how the regulatory agencies will proceed with these comments, policy reform advocacy should continue beyond the comments responding to the Notice. Community groups may continually comment on exams and merger applications,

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195 "Warren Unveils Historic Legislation to Confront America's Housing Crisis." Elizabeth Warren – Press Releases. September 26, 2018. <https://www.warren.senate.gov/newsroom/press-releases/warren-unveils-historic-legislation-to-confront-americas-housing-crisis>

write a letter to an agency or request to meet with agency staff at any time to provide input or advocate for reforms.

The National Community Reinvestment Coalition (NCRC) also remains an important avenue through which reforms or responses to the OCC's request for comment may be advocated. It is a member-based organization that provides its members with the resources and infrastructure to navigate the CRA and advocate for reforms. Community groups, particularly those focused on community wealth building approaches, can help advance the reforms in this working paper by first becoming a member and then, through its infrastructure, helping to channel calls for greater emphasis on the reforms outlined here and to legitimize any calls NCRC chooses to take on towards these ends. NCRC also hosts an annual conference for its members, which provides a formal way to advocate for certain reforms and a place for organizing work around such reforms. Also, while the recommendations here focus primarily on reforms to the CRA that improve its democratizing capacity, NCRC continues to publish reports that entail additional, more specific and still important reforms in their annual policy agendas for both the CRA and other laws and agencies concerning community investment.

The policy points presented here are largely summaries of those elaborated on in more detail in the "Rethinking the CRA as a community wealth building tool" section of Part 2. The primary policy aims, what regulatory body can act, and where advocacy efforts may be directed are included here, while more specific proposals under each policy point and lengthier discussion can be found in that section. The following section highlights how communities can help lay the groundwork for many of the proposed reforms—such as working to help bring awareness and build expertise in the community wealth building models (especially in low-income communities) and working towards a robust legal justification for expanding the CRA.

## Key reforms and ways to advance them

**1. Add community wealth building models to CRA criteria and expand on the definition of community development.** Such models could include cooperatives, land trusts, and municipal enterprises and others as outlined in The Democracy Collaboratives' *Cities Building Community Wealth* and *Financing the Inclusive Economy* reports. A redefinition of community development could entail expanding the definition in the Q&As from "activities that promote economic development" by financing small businesses and mortgages to include "activities that promote economic development; equitable, local, and collective ownership of assets; and cross-sector community collaboration by financing models and facilitating initiatives that meet these ends" within low- and middle-income communities. This definition would center communities more than the current one, which is more focused on a strict definition of small businesses.

### Who can act:

□ Communities, which can submit comments in response to the OCC's most recent Notice of Proposed Rulemaking supporting changing the definition of community development and adding additional performance criteria. Comments are due November 19, 2018.<sup>196</sup> NCRC has provided a template and instructions for how to submit a comment via their website, [ncrc.org/treasureCRA](http://ncrc.org/treasureCRA).

□ The regulatory agencies<sup>197</sup> can make changes to the criteria and the definition of community development (though the latter may be more difficult).

□ Congress can change the legislative language that defines community development.

<sup>196</sup> "Reforming the Community Reinvestment Act Regulatory Framework." Department of the Treasury, Office of the Comptroller of the Currency. August 28, 2018. P. 15. <https://www.occ.gov/news-issuances/bulletins/2018/bulletin-2018-24.html>

<sup>197</sup> The agencies with authority to issue regulations building on the CRA's original statutory language include the Office of the Comptroller of the Currency (OCC), which regulates national banks; the Board of Governors of the Federal Reserve System (FRB) which regulates state-chartered member banks, and Federal Deposit Insurance Corporation (FDIC) which regulates state-chartered nonmember banks.

Where to advocate:

- The OCC, through comments on the recently issued Notice of Proposed Rulemaking (see above).<sup>198</sup>
- During CRA exams: Here individuals and community groups can submit comments and strategically align their recommendations with the language of community wealth building (see the CRA community wealth building guide for how to submit comments), arguing the examined bank is not fully meeting the credit needs of communities. It is particularly important to note when community groups have approached the bank with projects associated with community wealth building models (such as cooperatives) and have been denied.
- Future Notices of Proposed Rulemaking and hearings: Organizations with a focus on community wealth building initiatives should prepare to make comments in future Notices of Proposed Rulemaking as well as hearings held by the agencies once they are announced. (See the CRA community wealth building guide for how to track hearing announcements.)

**2. Encourage regulatory agencies' community development divisions to connect banks with community groups and projects** (particularly ones geared towards community wealth building)—such as by providing Investment Connection events—and better integrate examiners with the research and staff of the community development divisions.

Who can act:

- Communities, by contacting the local community affairs divisions to request that they hold events similar to the Fed's Investment Connection events.
- The agencies' community development divisions, which could expand the use of such Investment Connection events and may work to better integrate examiners with the research and staff of the community development divisions.

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198 "Reforming the Community Reinvestment Act Regulatory Framework." Department of the Treasury, Office of the Comptroller of the Currency. August 28, 2018. p. 15. <https://www.occ.gov/news-issuances/bulletins/2018/bulletin-2018-24.html>

□ The agencies' federal administrative bodies, which can help facilitate and may be necessary in integrating the roles of examiners and community affairs officers.

Where to advocate:

- Agency conferences, particularly the Federal Reserve's annual conference on community development. These conferences present opportunities to advocate for reforms to the Community Reinvestment Act, particularly to call regulators' attention to community wealth building models and the importance of Federal Reserve district banks playing a greater role in facilitating dialogue on the local level (through initiatives similar to the Investment Connection event).
- Federal Reserve banks: Community groups in the district of the Kansas City Fed (i.e. Wyoming, Colorado, Nebraska, Kansas, Oklahoma, and parts of Missouri and New Mexico) may be particularly able to provide Investment Connection events given that the program was piloted in this district. Community groups outside this district could request that similar events be offered by their district banks and use the Kansas City Fed's precedent as encouragement.

- The OCC: Comments on reforms to the performance context may be submitted in response to the OCC's most recent Notice of Proposed Rulemaking.
- Regulatory hearings held by the agencies are another opportunity to advocate for a greater role for the agencies' community development divisions.

**3. Standardize the performance contexts to streamline exams and facilitate public input.** Doing so could consolidate the data and knowledge already held at the regulatory agencies, along with community input, to be used for a more standardized and community-based assessment of bank performance (versus examiners independently writing a new performance context for each exam).

Who can act:

- Communities, which may submit comments in response to the OCC's most recent Notice of Proposed Rulemaking on reforms to the performance context.

The agencies' federal administrative bodies, which in coordination with the U.S. Census Bureau can work together to consolidate relevant data and other information.

Communities, which can prepare their own performance context analyses to be put towards current and any future standardized performance analyses.

Where to advocate:

OCC Notice of Proposed Rulemaking (see above).

Future Notices of Proposed Rulemaking and hearings: Submitting comments to future hearings held by the agencies, and future Notices of Proposed Rulemaking, are likely the main way to advocate for standardized performance contexts.

**4. Improve the overall transparency of the law**—e.g. its accessibility to the public—such as through more detailed data collection (particularly of the demographic of borrowers and the type of business financed, if community wealth building approaches are to be added), regular and public facing CRA exam schedules, and improvement of agency websites (discussed further in the next section).

Who can act:

Communities, which may submit comments in response to the OCC's most recent Notice of Proposed Rulemaking on the type and frequency of data collection and reporting by banks.

Individual regulatory agencies, which can ensure their websites are up to date and that information regarding the CRA is more organized and easily accessible.

The regulatory agencies' federal administrative bodies, which will be necessary for data collection improvements and in providing an easily accessible CRA exam schedule.

Where to advocate:

OCC Notice of Proposed Rulemaking (see above).

Individual regulatory agencies: Pressuring the

agencies to improve and update their websites can be done through future hearings, notices of proposed rulemaking, or other direct correspondence.

**5. Redefine assessment areas** to include areas of significant financial activity (outside of bank branches) and expand the CRA to all financial institutions or a more limited subset, such as online financial companies, mortgage affiliates, and credit unions.

Who can act:

Communities, which can submit comments in response to the OCC's most recent Notice of Proposed Rulemaking on redefining communities and assessment areas.

Federal agencies, which can direct examiners to consider certain assessment areas as being subject to full scope review (even if the area does not include bank branches).

Federal agencies, which may be able to expand CRA to mortgage lenders that are affiliates in the same bank holding company as a CRA-covered institution.

Congress, which can make legislative changes to expand the CRA to other financial institutions.

Where to advocate:

OCC Notice of Proposed Rulemaking (see above).

Regulatory agencies: Communities may contact the agencies directly at any time, or use future hearings held by the agencies as an opportunity to advocate for the inclusion of certain assessment areas.

Congress: Communities may put pressure on congressional representatives to expand the CRA to other financial institutions in future proposed legislation. Such legislation ideally would develop a sound legal justification for expanding the public purpose argument of the CRA beyond depository institutions (discussed further in this section).

**6. Improve the enforcement mechanisms**, either through the current CRA regulatory framework (such as im-

provements to transparency and enforcement around merger applications) or by instituting stricter financial penalties in the form of fines or divestments.

Who can act:

- Regulatory agencies, which can address improvement to the transparency and enforcement around merger applications.
- Congress, which would have to institute stricter penalties via legislative change.

Where to advocate:

- Agency regulatory hearings, which are an opportunity to advocate for improved transparency and enforcement around merger applications.
- Congress, where communities can call on their representatives to legislate stricter penalties.
- Accompanying legislation, agencies and reinvestment institutions.

In addition to CRA reform, the following points support reinforcing existing legislation and regulatory agencies as well as other financial institutions that can support community investment. It is of course not a complete list, but one that highlights the main laws and tools that can help increase economic security and bolster community investment in communities.

**1. Defend and bolster the Dodd-Frank Act and the Community Financial Protection Bureau** (discussed more in the next section).

Who can act:

- Communities, which can pressure congressional representatives to resist efforts to weaken Dodd-Frank and the CFPB.
- Voters, who can base their choice of elected officials based on whether they support strengthening existing banking regulation and the appointment of agency directors who share similar aims.
- Congress, which is ultimately responsible for Dodd-Frank and the CFPB.

Where to advocate:

- Offices of congressional representatives, where advocacy for resisting efforts to weaken current banking regulation is best directed.

**2. Defend and bolster programs and policies related to community investment concerns** and associated with agencies such as the Federal Housing Authority, Fannie Mae and Freddie Mac, the National Housing Trust Fund, Capital Magnet Fund, and the Department of Housing and Urban Development.

Who can act:

- The respective regulatory agencies, which would be responsible for implementing many of the reforms recommended by NCRC in its annual policy agendas.

Where to advocate:

- National Community Reinvestment Coalition: NCRC regularly reviews improvements to such policies and programs. Communities may become members of NCRC to help channel advocacy efforts for aspects of those laws that affect their interaction with community investment efforts.

**3. Establish public banks** (i.e. government owned banks) at the city, state, or national level.

Who can act:

- City and state governments, which can establish public, or government-owned, banks modeled after the Bank of North Dakota, the only public bank in the U.S.). Several states have already begun this process by introducing bills to either study public banks or establish a government-owned bank.<sup>199</sup>

Congress, which could appropriate funds to establish a public bank at the national level.

<sup>199</sup> Morton, Heather. "Many States see the Potential of Public Banking." *The New York Times*. October 1, 2013.



Where to advocate:

Local and state government: Communities may organize to put pressure on current or campaigning city or state representatives to establish public banks.

Congress: Communities can urge Congress to establish a community investment or cooperative bank, especially during a relevant political moment (such as the aftermath of a financial crisis).

**4. Establish community or cooperative development banks** and community-focused credit unions at the city, state, or national level.

Who can act:

Communities, which can organize locally to establish community-focused credit unions or community development banks.

Congress, which could appropriate funds to establish a community investment or cooperative bank in the way it did with the National Cooperative Bank.

Where to advocate:

Local developers and funders: Communities can coordinate with them to establish a credit union focused on the needs of the surrounding community or a local bank with a particular community development mission.

Congress: Communities could use a relevant political opportunity to pressure Congress to establish a community investment or cooperative bank.

### In the meantime: Defending the CRA and laying the groundwork

Regardless of what avenues for reform are available come 2020, basic work needs to happen in the meantime to lay the groundwork for investment in community wealth building models. These efforts involve:

- Defending the CRA from efforts to remove or weaken it.
- Building up best practices for starting, growing, and financing community wealth build-

ing best practices and alternative community investment models.

- Organizing communities to be central to the development planning process.
- Increasing transparency to facilitate public engagement with the CRA.
- Laying the legal groundwork for extending the “public purpose” requirement.

### *Defending the CRA*

Of first importance to CRA reform efforts is keeping the CRA in existence and defending it against such efforts to remove or weaken it, such as proposals to maintain or even raise the asset size thresholds for small and intermediate-small banks.<sup>200</sup> The continued existence of the CRA allows both banks and communities to continue to operate within a framework for community investment, and provides the basis for reforms that a separate law might be modeled on.

Particularly as the CRA undergoes regulatory review by the agencies under the current administration and requests for public comment about particular reforms are issued, the National Community Reinvestment Coalition (NCRC), an association representing over 600 community reinvestment organizations, remains a critical resource for policy advice on which proposed reforms would weaken or strengthen the CRA. (See in particular, their recent comments on the OCC’s proposed metric-based performance evaluation system).<sup>201</sup> For the last several decades, NCRC has remained the primary defender the CRA by holding annual conferences for its members, providing training sessions, publishing policy memos, testifying before Congress, and working with regulators to strategize around policy reform. Opportunities to become involved with NCRC’s work—such as becoming an organizational member or attending the annual conference—are detailed on their website. Furthermore,

200 “2017 Policy Agenda: Investing in a Just Economy.” National Community Reinvestment Coalition. 2017.

201 Silver, Josh. “The One Big CRA Fight Over the One Ratio.” National Community Reinvestment Coalition. August 21, 2018. <https://ncrc.org/the-one-big-cra-fight-over-the-one-ratio/>

pressure on congressional representatives and regulatory agencies to maintain the CRA can be made should there be attempts to weaken it.

Similarly, efforts to defend key financial regulatory provisions, namely Dodd-Frank, from being seriously weakened are necessary to maintain a stable financial system that does not strip wealth gains or engage in other forms of discriminatory or exploitative practices. Though not essential to the CRA itself, Dodd-Frank seeks to help protect communities from the destructive forces of financial crisis and prevent the use of taxpayer money for bailouts, and the Consumer Financial Protection Bureau was created to defend communities from abusive financial practices.

The primary way to support such laws is through pressure on representatives should attempts to weaken or dismantle Dodd-Frank come before Congress. Though no formal group exists to defend Dodd-Frank as a whole, the NCRC also works to provide information on and in defense of the Consumer Financial Protection Bureau.

### *Building up community wealth building best practices and community investment models*

In addition to defending existing legislation, communities must also work to lay the groundwork to facilitate capital going towards more community wealth building models. As Me’Lea Connelly of the Association for Black Economic Power highlighted in the discussion in Part 2, efforts to reform the CRA should be matched with double the effort on readying communities to use CRA financing towards projects that keep capital in communities.

Two main barriers impede the success of this, both of which were highlighted in Part 2. The first is that, despite growing interest in and success of community wealth building, there is still a broad lack of understanding on both the financing and community development side of the models, policies, and best practices of these approaches. The second barrier is the dilemma of preparing underinvested communities to meet initial capital requirements and of putting

communities in a position to put capital towards collectively identified projects.

Elevating an understanding of the community wealth building model has precisely been the work of The Democracy Collaborative, among many organizations, over the last decade. The 2016 *Strategies for Financing the Inclusive Economy* report outlines current methods of financing wealth building models—such as cooperatives, employee stock ownership plans, social enterprises, hybrid enterprise, and municipal enterprises—“to demystify the financing of broad-based enterprise.”<sup>202</sup> The report cites the importance of specialized lenders, or lenders familiar with such alternative models, such as cooperative loan funds—some of which are certified CDFIs (e.g. Cooperative Fund of New England, Local Enterprise Assistance Fund, and Shared Capital Cooperative)—or cooperative banks, such as CoBank or the National Cooperative Bank. It further discusses the importance of philanthropic and government financing for starting up such businesses in low-income communities. The 2014 *Policies for Community Wealth Building* report covers local policies that facilitate wealth building models, such as land trusts, responsible banking ordinances, and city land banks.<sup>203</sup> Building up these financing institutions (by becoming members to build their network and capital base or learning from and expanding the use of their strategies) and local policy reforms will be critical to support the development of these wealth building models.

Most importantly, a wealth of information, experience, and skill sets exists in communities across the country among those already working within these models. How to strategically bring those voices to the table to build relationships and spread information on these models is the subject of the *Sparkling the conversation in your community: A DIY guide to planning your own community wealth building summit* report.<sup>204</sup>

202 Duncan, Violeta, Dubb, Steve, Kelly, Marjorie. *Strategies for Financing the Inclusive Economy*. (The Democracy Collaborative. September 2016).

203 *Policies for Community Wealth Building: Leveraging State and Local Resources*. (The Democracy Collaborative. September 2014).

204 Porter, Justin. “Sparkling the conversation in your community: A

Moreover, many communities have local cooperative coalitions or councils already working to build a network of professionals, share resources, and bring about local policy reforms. The *Cities Building Community Wealth* report provides case studies of communities that have made such reforms.

Outside of this work, best practices down to the level of instructional guides on how to start a housing co-op, anti-oppression training for existing organizations, or case studies on worker co-op conversions exist on various organizational websites (such as the North American Students of Cooperation Organization and U.S. Federation of Worker Cooperatives). The CRA and community wealth building guide accompanying this report compiles a list of organizations and resources available towards this end. Overall, building awareness of these models will help address current barriers to investment from traditional lenders.

Furthermore, greater understanding of best practices and organizing strategies for community-focused cooperatives, community development banks, and particularly public banks (given their limited representation in the U.S.) is needed around these models. The Public Banking Institute exists to provide educational resources on public banking. Meanwhile, as states begin to explore public banks, policy briefs are being written on how to go about instituting them.<sup>205</sup> Moreover, given that such models would pertain primarily to depository institutions, cooperatives, or public models for other financial institutions (such as credit card companies or payday lenders) ought to be explored further.

### *Organizing communities to be central to the development planning process*

A key component of the community wealth building approach is participatory planning and putting

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DIY guide to planning your own community wealth building summit." The Democracy Collaborative. January 2017.

205 Figart, Deborah. "Exploring a Public Bank for New Jersey: Economic Impact and Implementation Issues." Stockton University. April 2018. <https://stockton.edu/hughes-center/documents/2018-0326-exploring-a-public-bank-for-new-jersey-economic-impact-and-implementation.pdf>

communities at the center of the development work, particularly those traditionally excluded from the development process. There can, however, be barriers to this, given that historically disenfranchised communities lack the resources (i.e. time, money, social capital, etc.) and infrastructure to be able to meet developers halfway to refine the objective of projects to a given community's needs and to allow the community to take ownership of the development project. Community development corporations (CDCs) are an important connecting point for pulling capital into community-based projects, though their accountability to communities can vary, and by acting as an intermediary they can sometimes (though not in all cases) allow banks to be more hands-off.

However, new initiatives are emerging to begin the development process from within communities to better match capital directly with community needs and projects, and for the communities themselves to drive the development projects. Designing the WE is a social impact design studio that started WELabs, community-based development labs, in the Bronx, New York and Trenton, New Jersey, and is looking to expand into three small towns around the country. Director and co-founder April De Simone explains:

"[The WELab] is a public library and an incubator shrouded in design thinking so that when banks are interested in understanding the local contexts and needs us, this is a plug-in place with an anthropological lens that can be used for applied CRA funding. That way it's not just project-specific—it's a living archive living in continuum with the community."<sup>206</sup>

The WELabs, first launched in 2015, are situated within the communities they intend to serve, operating as both a community space and training center for community members to conduct surveys, identify community needs, and bring community projects into reality. For instance, through the Bronx WELab, a youth group at the Mary Mitchell Family and Youth Center in the Bronx worked to identify the need for

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206 Interview with April De Simone.

healthier and affordable food options in their community, and decided a low cost, membership-based community kitchen that provided food and cooking classes was the best solution. The project and research results are pulled together into the WELab's archive for others to access, to determine what has and has not worked and what the feedback was from the community. The benefit, as de Simone notes, is that "[These] spaces become the gateway where projects are happening within the community rather than bringing in a consultant... The goal is to be stewarded locally, with [local] people using their skill sets."<sup>207</sup>

These spaces are what de Simone sees as missing in too many CRA development projects. "A huge potential with CRA has to be in the democratizing of the planning of a community," she says. To do so, "we need to create better transparency and allocation of plug-in points, so that we can see more of the projects that we're passionate about."

The WELabs serve as plug-in points connecting capital to communities, and not just on a one-time basis. As De Simone notes, "It can't be a one-time conversation. There has to be a consistent check-in to say, 'How are we using CRA money in this local community to create impact, and how can we track that?'"<sup>208</sup>

Proliferating this model could help bridge the disconnect between banks and communities, overcoming the uncertainty of lending to low-income communities and providing the infrastructure for developing-community-centered project ideas. In the meantime, de Simone calls attention to the need for financing for the WELab as a model in itself: "There's a problem of connecting impact investing to this—[to get investors to] not just invest in the project that comes out of the process but also the process itself."<sup>209</sup>

### *Increasing transparency*

The complexity of the CRA's regulatory framework and the uncertainty about when and what avenues are

available for reform through the regulatory agencies makes public input difficult. Many have advocated repeatedly for greater clarity from the regulatory agencies, to increase transparency by consolidating and cleaning up agency websites to improve access to information and input, and to communicate more openly about exam schedules and hearings.<sup>210</sup> Yet, as of the writing of this paper, many government websites pertaining to the CRA remain buried in other agency websites, are broken or are out of date.

The CRA community wealth building guide accompanying this working paper seeks to consolidate resources around the CRA's history and function as well as resources that facilitate public advocacy for reform. Additional support from advocacy organizations (such as NCRC) to publish policy agendas or research reports and maintain an up-to-date directory on their websites with relevant links to help the public access or provide input on data, exams, or merger reviews could facilitate public understanding and engagement. Advocacy organizations are arguably best positioned to do this work, being that they have years of experience working with the legality and mechanisms of the CRA, as well as monitoring the regulatory agencies that oversee it. Ideally the regulatory agencies would take it upon themselves to do this work, but in the interest of catalyzing reforms, advocacy groups making information more accessible in the meantime could help build interest and involvement.

### *Extending the "public purpose" requirement*

All of the organizing efforts in this paper are put forward to help lay the intellectual groundwork for increasing the capital that goes into community wealth building initiatives, ideally via legislation that expands the CRA. Laying that groundwork is equally important for establishing the argument for the broader law. What Part 2 highlighted is that all too often the argument for expanding the CRA to all financial institutions is that they all benefit from an "implicit guar-

207 Ibid

208 Ibid.

209 Ibid.

210 See primarily "Testimony of Josh Silver, Senior Advisor, NCRC Regarding the Regulatory Review Mandated by the Economic Growth and Regulatory Paperwork Reduction Act (EGRPRA)." National Community Reinvestment Coalition. December 2, 2015.

antee”; not only do commercial banks have access to FDIC insurance, but non-commercial banks also received government-supplied insurance in the form of bailouts and stimulus packages to keep them (and the economy) afloat during a crisis, as the 2008 financial crash demonstrated. This logic, though true, only reasserts a fact that other legislation is attempting to invalidate—namely, the provisions in the Dodd-Frank Act designed to remove that implicit guarantee.

Moreover, this logic misses the broader point that there is arguably *a priori* government support for all private institutions, and subsequently the functioning of the nominal “free market,” in the form of courts that uphold private property rights and contracts, and a central bank that provides such services as providing the nation’s currency and managing the money supply. This logic runs against the false dichotomy too often present in economic and public discourse that a government policy that seeks to correct market failures is a “government intervention” in what is and would otherwise be a “free market.”

Aside from the need to assert a more fundamental public purpose in order to legally extend CRA authority to all financial institutions, this distinction is important to clarify free market rhetoric, too often prevalent in policy debates, that considers government and market as separate, and views the government as intruding on normal free-market functioning. This ideology and rhetoric in turn inhibits arguing for policies that state a more fundamental public-purpose function of private institutions (especially financial institutions) and that would support more development of “next system” solutions and business models. They would be justified by sound legal arguments based on the fact that “governments don’t ‘intrude’ on free markets; governments organize and maintain them. Markets aren’t ‘free’ of rules; the rules define them.”<sup>211</sup> This clarification is where the implications for effective economic policy lie.

211 Reich, Robert. “The Myth of the ‘Free Market’ and How to Make the Economy Work for Us.” Blog post on *Robert Reich*. September 16, 2013. <http://robertreich.org/post/61406074983>

This paper has highlighted how this market logic impedes effective economic policy. Fortunately, the CRA as it was originally formulated in 1977, and more significantly the Federal Reserve Board of Governors’ stated interpretation of bank holding company law in 1972, made some progress towards defining a public obligation for banks. A stronger assertion is necessary, however, to compel a public purpose for all financial institutions in a broader law. Such an assertion would extend the public purpose requirement for financial institutions not just because the government provides a backstop in the event of market failure, but because the government provides the infrastructure to support the so-called free market’s very existence. Such an assertion could build on the “public convenience and necessity” argument applied to industries serving the public (e.g. communications and power companies) that in part informed the original CRA organizers’ drafting of the legislative language.

### **A stronger justification for CRA expansion could involve extending a ‘public convenience and necessity’ argument to financial institutions.**

Needless to say, more work needs to be done to build up this argument and spread awareness of the false dichotomy between “government” and “market” that keeps a redefinition of this relationship off of political or policy platforms. Without this work, a broader law will be seen and attacked—as strong economic policies historically have been—as government impeding the market from doing its work. In terms of community investment, this would mean that financial services will continue to expand outside of the reach of CRA reform, and thus out of the reach of low-income communities and communities of color and of long-term, wealth building development projects.

## Conclusion: Toward a CRA that puts community first

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The Community Reinvestment Act has remained a remarkably resilient piece of legislation over the last 40 years. Since it was passed in 1977 with simple language allowing it to be tacked onto a housing bill, it has spurred billions of dollars of investment into communities that likely would not have occurred in its absence.

Emerging out of community organizers' efforts to spur lending and investing in the Black community, other communities of color, and lower-income communities—to go beyond concurrent anti-discrimination legislation in mandating a more fundamental public purpose of banks—the CRA can foremost be attributed with overcoming the initial hurdle of bringing investments into redlined communities. It called on commercial banks to do so given that the deposits they collect and profit they make from via loans and investments are afforded by their public charter and are secured by government guarantees such as federal deposit insurance (and now, as evidenced in the 2008 financial crisis, bank bailouts). Most importantly, it *continues* to motivate billions of dollars of loans and investments into communities that may not occur otherwise.

However, the impact of the lending and investing the CRA has spurred has been limited by both the type of investment and limited amount of investment relative to the banks' overall capacity. The

CRA emphasizes small business lending, home ownership, and affordable housing without specifications on the type of business ownership (private, collective, local, or public) or the long-term impact (whether or not the development benefits will persist for more than a few years or actually serve the community it intends to serve). Criteria allowing investments in community development corporations (CDCs) and community development financial institutions (CDFIs) have built a network of community-based institutions, though arguably at the cost of allowing banks to be relatively hands off and eschew the public purpose obligation they were originally intended to take on. In the end, communities of color remain underinvested, and despite regulatory guidance CRA-financed developments still too often lead to the target community being displaced as property values and rents rise.

Meanwhile, non-CRA covered institutions (e.g. non-bank and non-affiliate mortgage companies as well as non-depository investment banks, mutual funds, or hedge funds) now play a greater lending and investing role in the communities the CRA was originally enacted to serve. Perhaps most importantly, legislative and structural changes in the banking industry have moved banks away from being more centered in communities. Such changes increasing the size and complexity of banks have also made it so that as one

division of a bank is lending and investing in lower-income communities to fulfill its CRA requirements, another division is engaging in exploitative lending practices that strip wealth gains from the very communities served by the CRA or imperil those communities through the kind of reckless lending and investments capable of sparking a financial crisis. The most recent Wells Fargo CRA exam results presented in the introduction of this working paper highlights this contradiction at the heart of the present system that confronts major policy reform.

None of these shortcomings are the fault of the CRA per se. Rather, structural and ideological shifts occurring in the US political economy over the last several decades have presented a challenge to CRA-motivated investments while also impeding the economic and banking reform necessary to address the countries' most endemic social ills—economic inequality and insecurity, perennial economic crisis, and environmental degradation, to name just a few. With political interests becoming more structurally and ideologically aligned with private, free-market interests, the democratic capacity of the political system has become less responsive to the needs of those continuing to be pushed to the margins. Consequently, CRA reform has also been stalled by regulatory fears that drawing too much attention to it might lead to its ruin, in addition to regulators' limited capacity to make major reform outside of the initial legislative language (such as the inability to expand the CRA to include non-depository institutions or implement stricter enforcement mechanisms).

These same structural and ideological barriers that present a challenge to policy reform are also the reason so many communities have turned to themselves for solutions. With decreasing capacity for meaningful political and economic participation in the present system, more and more communities across the country are taking up models and approaches that bring more democratic ownership and control of assets at the local level, such as cooperatives, social enterprises, and land trusts. They are forming connections and initiatives locally by establishing

community wealth building offices and using anchor institutions such as universities and hospitals to grow markets for locally produced goods. They are establishing a new pattern of political economic relationships—planting the seeds for a new system, beginning locally. The Democracy Collaborative has brought these models and approaches together under the community wealth building framework in reports such as *Cities Building Community Wealth* to raise awareness of their success in bringing greater economic participation and stability in communities across the country, and to bring the very idea of system change into public discourse.

**More communities across the country are taking up models and approaches that bring more democratic ownership and control of assets at the local level. They are establishing a new pattern of political economic relationships—planting the seeds for a new system, beginning locally.**

The current CRA regulatory framework presents many opportunities to make it a more effective community development tool and to align CRA-related investments and lending with the community wealth building framework and the development models therein. Moreover, the fact that the depository asset base of banks now exceeds \$12 trillion suggests that there are significant resources still untapped within CRA-covered institutions, let alone the broader financial system, for greater community reinvestment.

However, in order for the CRA to be a more effective tool, long overdue reforms need to be made. The reforms included in the policy agenda of this working paper could go far in facilitating such alignment

of CRA-related activity and the community wealth building framework by such means as building on the current CRA qualifying criteria, changing the community development definition, encouraging greater engagement by the regulatory agencies, and improving the overall transparency to further facilitate public input. They could also motivate the financial sector to devote a greater portion of its capacity towards CRA-related activities by enacting enforcement mechanisms that make banks more accountable to communities, expanding the definition of assessment areas, and expanding the law to non-depository financial institutions. Though the opportunities to pursue such reforms exist at different levels—from within the current CRA framework and the administrative agencies to Congress—making the entire financial sector more centered in and responsive to communities is a fundamental requirement of holistic reform.

Given the structural and ideological barriers facing such sweeping reforms and the potential that such reforms may not go far enough in shifting banks' focus to community investment in a holistic way, other community investment institutions (such as public

banks or community development banks) should be considered alongside CRA reform. Meanwhile, existing laws regulating the financial industry must be defended to protect wealth gains from being stripped away by the next financial crisis. For this reason, the policy agenda includes recommendations not only specific to CRA reform, but also for creating alternative financial institutions and defending or strengthening existing financial regulations.

Ultimately, the Community Reinvestment Act and its accompanying regulations and institutions remains a critical and vital resource for community reinvestment. As reform opportunities emerge in both the near- and longer-term, communities—organizers, lenders and local policy leaders—can advocate to make it an even more effective tool among many to advance a community wealth building approach to community development. In doing so, the CRA will not only help promote economic security and inclusion but will help plant the seeds of a new system—one focused on building up local relationships, fostering local ecologies, and democratizing the ownership and control of assets at the community level.



# The Next System Project

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The Next System Project is an ambitious multi-year initiative housed at The Democracy Collaborative that is aimed at thinking boldly about what is required to deal with the systemic challenges the United States faces now and in coming decades.

Responding to real hunger for a new way forward, and building on innovative thinking and practical experience with new economic institutions and approaches being developed in communities across the country and around the world, the goal is to put the central idea of system change, and that there can be a “next system,” on the map.

Working with a broad group of researchers, theorists, and activists, we seek to launch a national debate on the nature of “the next system” using the best research, understanding, and strategic thinking, on the one hand, and on-the-ground organizing and development experience, on the other, to refine and publicize comprehensive alternative political-economic system models that are different in fundamental ways from the failed systems of the past and capable of delivering superior social, economic, and ecological outcomes. By defining issues systemically, we believe we can begin to move the political conversation beyond current limits with the aim of catalyzing a substantive debate about the need for a radically different system and how we might go about its construction.

Despite the scale of the difficulties, a cautious and paradoxical optimism is warranted. There are real alternatives. Arising from the unfor-giving logic of dead ends, the steadily building array of promising new proposals and alternative institutions and experiments, together with an explosion of ideas and new activism, offer a powerful basis for hope.

Learn more at [thenextsystem.org](https://thenextsystem.org).



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