

June 19, 2019

Submitted Electronically

The Honorable Jelena McWilliams
Chairman, Federal Deposit Insurance Corporation
550 17th Street NW
Washington, DC 20429

The Honorable Jerome Powell
Chair, Board of Governors of the Federal Reserve System
20th Street & Constitution Ave., NW
Washington, DC 20551

The Honorable Joseph Otting
Comptroller of the Currency, Office of the Comptroller of the Currency
400 7th Street SW, Suite 3E-218
Washington, DC 20219

**RE: The Pending Draft Joint Agency Community Reinvestment Act Reform
Proposal (the “Proposal”)**

Dear Ms. McWilliams, Messrs. Powell and Otting:

On behalf of the Bond Dealers of America (“BDA”)¹, we offer comments in response to recent statements made by the Federal Deposit Insurance Corporation (“FDIC”) Chairman Jelena McWilliams that a draft joint agency proposal to reform the Community Reinvestment Act (“CRA”) is forthcoming. The anticipated proposed rule is the outcome of the Office of the Comptroller of the Currency’s (“OCC’s”) Advanced Notice of Proposed Rulemaking (“ANPR”) entitled “Reforming the Community Reinvestment Act Regulatory Framework,” and the many comments received thereon.² We recognize that the comment period for the ANPR has closed. However, in anticipation of the forthcoming proposed rule, we wish to address an issue that we believe is important

¹ The Bond Dealers of America is the only Washington, D.C.-based trade association representing the interests of “Main-Street” investment firms and banks whose primary focus is the U.S. fixed income markets.

² See, 83 Federal Register 45053 (September 5, 2018).

to our membership as well as to the main street community banks that our membership serves.

Specifically, the ANPR raised the issue of whether CRA eligible targeted loan backed securities, such as residential housing or multifamily dwelling loan backed securities (“TMBS”) should be limited or excluded from CRA consideration.³ We believe that limiting the eligibility for CRA credit, or entirely excluding these securities from eligibility for CRA credit, would effectively destroy both the primary and secondary markets for these securities and deprive community banks of a significant means of achieving their CRA goals. It would also adversely affect the availability of credit in the low- or moderate -income (“LMI”) communities that now benefit from the liquidity provided by these securities.⁴

The BDA believes that limiting or terminating an institution’s ability to get CRA credit from TMBS will make it substantially more difficult for many community banks to fulfill their CRA obligations and would virtually eliminate the market for TMBS.

Most residential mortgage backed securities are backed by loans scattered throughout the country. MBS is a useful investment for many banking institutions given its relative safety, yield and marketability. TMBS, whether private or agency backed, however, precisely because they lack diversity, would not be an attractive investment for banks but for their CRA eligibility. As noted by the Federal Reserve Bank of San Francisco, targeted affordable housing mortgage backed securities are “created with loans to LMI borrowers in specified geographies. As a ‘qualified investment,’ the MBS should include loans in an institution’s assessment area or in a statewide or regional area that includes the assessment area. At least 51 percent of the dollars in the MBS should be in loans to LMI borrowers, although in most cases the total is 100 percent.”⁵

Some of our members have noted that a good portion of their business in the CRA space comes from community banks that lack the opportunity to make direct loans to their LMI constituencies because the market for such loans is highly competitive given the presence of nationwide bank and nonbank competitors. TMBS provides a valuable alternative means of meeting their CRA obligation. Moreover, TMBS is an attractive investment precisely because the need for CRA eligible investments has created an efficient secondary market for such securities. Our members have often seen multiple bids for TMBS that has come to market both at origination and on resale. The limitation, or

³ Question 18 of the ANPR asked the following question: “18. Should consideration for certain activities that might otherwise qualify as CD be limited or excluded? For example, how should investments in loan-backed securities be considered?”, 83 Federal Register 45053, at 45058.

⁴ Although this letter focuses on single and multifamily residential mortgage backed securities, other asset classes such as small business loans in LMI areas would be similarly adversely affected.

⁵ Federal Reserve Bank of San Francisco. “CRA Investment Handbook.” March 2010, at p. 22.

elimination of, CRA credit for these securities would effectively destroy both the primary and secondary markets for these securities.

By so doing, it would also limit access to credit by LMI borrowers by reducing the velocity of available credit. The supply of financing for affordable housing is increased by investors, including community development financial institutions (CDFIs), community development agencies, and state housing agencies. As pointed out by the San Francisco Fed: “CRA-qualified MBSs increase the supply of affordable housing. MBS dealers pay a premium to originators for the low- to median-income (LMI) loans they sell, giving originators an incentive to create additional LMI lending opportunities in communities, which is the essence of the CRA. Banks that purchase MBS pools from dealers support this affordable housing initiative. *Investors increase the supply of financing for affordable housing through this product by leveraging investment in affordable housing from nondepositories and by creating incentives for loan originators.*” (Italics supplied.)

The BDA believes that the potential for abuse of TMBS is rare and limited and easily addressed by supervisory means rather than by impairing the marketability of these securities.

Our members have not seen situations in which community banks have purchased, sold and repurchased TMBS to inflate their CRA ratings, and believe this would be a rare occurrence. If such abuse occurs, it would be apparent on examination, and can be addressed solely with the offending institution rather than by placing limits on an entire class of securities. The current CRA Questions and Answers (“Q & As”) deal with the similar situation of loan participations, stating that “As with other loan purchases, examiners will evaluate whether loan participations purchased by an institution, which have been sold and purchased a number of times, artificially inflate CRA performance.” In general, the Q & As provide that “Examiners will apply the performance criteria reasonably and fairly, in accord with the regulations, the examination procedures, and this guidance. In doing so, examiners will disregard efforts by an institution to manipulate business operations or present information in an artificial light that does not accurately reflect an institution’s overall record of lending performance.”⁶

We believe that any action taken by the agencies to address this potential abuse should avoid impairing the markets for TMBS. The effect of any such impairment would be significantly adverse to our members that participate in this market, but more importantly from a societal standpoint, it would have an adverse effect upon the community banks that are their customers, and, in particular, the LMI areas that now benefit from the availability of credit afforded by these investments.

⁶ See Q & As .21(a)—1 and .22(a)(2)—6, at 81 Federal Register 48505, at 48534 and 48537 (July 25, 2016).

* * *

Thank you for considering these comments.

Sincerely,

A handwritten signature in blue ink that reads "Mike Nicholas". The signature is written in a cursive style with a prominent initial "M".

Mike Nicholas
Chief Executive Officer