

OCC Brings Common Sense to CRA Ratings

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The OCC's recent revision to its Community Reinvestment Act examination and ratings policies is a welcome first step in a long overdue and much needed rethink of how supervisors might modernize the CRA so that the statutory goal of helping underbanked communities can be met in the digital era. The new policy requires a direct relationship between a discriminatory or illegal credit practice and the bank's CRA lending activities before the bank's CRA rating is affected. Since CRA guidance is typically interagency, it is to be hoped that the Federal Reserve and the FDIC will reframe their CRA guidance in a similar manner.

The policy reframes how a bank's CRA examination and rating would be affected by evidence of discriminatory or illegal credit practices that do not directly relate to the bank's CRA lending activities.^[1] The OCC set out two common sense principles to guide examiners:

- Principle #1: "There must be a logical nexus between the assigned rating(s) and evidence of discriminatory or other illegal credit practices in the bank's CRA lending activities to ensure alignment between the rating(s) and the bank's actual CRA performance."

If the examiner finds a direct relationship between evidence of discriminatory or illegal credit practices and the bank's CRA lending activities, then the examiner must assess the extent and strength of such evidence to determine what action may be warranted. The examiner must consider the bank's actual CRA performance, on the one hand, and the volume of customers harmed and egregiousness of the discriminatory or illegal credit practices, on the other. A downgrade of the bank's composite CRA rating "should be supported by strong evidence of quantitatively and qualitatively material instances of discriminatory or illegal credit practices directly related to CRA lending activities that have resulted in material harm to customers." The OCC also stated that its policy going forward will be generally not to lower a bank's CRA composite or component rating by more than one rating level based on evidence of related practices that do not amount to noncompliance with the bank's CRA lending obligations.

- Principle #2: "Full consideration is [to be] given to the remedial actions taken by the bank."

OCC examiners must consider the full array of corrective actions taken by a bank, including the cumulative impact of supervisory or enforcement actions taken against the bank, the progress to remediate the issues underlying such actions, and whether the actions are directly related to the bank's CRA activities and performance. If the bank has remediated or taken appropriate corrective actions to address the evidence of discriminatory or illegal credit practices, the bank's rating would not be lowered based solely on the existence of the practice before the CRA evaluation. The OCC stated that giving banks credit for remediation actions will ensure that a CRA rating does not penalize a bank for practices that have already been, or are in the process of being, remediated.

The OCC's clarification applies only to national banks, federal savings banks and federally licensed branches of foreign banks. It does not apply to state-chartered banks. It will be interesting to see whether the Federal Reserve or the FDIC issues similar common sense principles for CRA examinations and ratings for state-chartered banks.

Tailoring CRA examinations to the original intent of the statute should help regulators finish CRA examinations more quickly. It should eliminate the multi-year delays in issuing CRA ratings that have been experienced in recent years. And most crucially, as the Secretary of the Treasury noted in the June 2017 report on banks and credit unions:

"It is very important to have the benefits arising from banks' CRA investments better align with the interest and needs of the communities that they serve and to improve the current supervisory and regulatory framework for CRA. Treasury

expects to comprehensively assess how the CRA could be improved to achieve these goals, which will include soliciting input from individual consumer advocates and other stakeholders. Aligning the regulatory oversight of CRA activities with a heightened focus on community investments will become a high priority for the Secretary.”

Getting started on a digital era CRA, including reconsidering how assessment areas are defined in light of mobile and internet banking, is a high priority. Removing other supervisory elements that have crept into the CRA examination and ratings processes will also eliminate a distraction from that important social goal. It will be interesting to see what the U.S. Department of the Treasury may recommend regarding the CRA in any future reports on financial regulatory reform.

Law Clerk Johnathan Nixon contributed to this post.

[1] The CRA is intended to encourage financial institutions to help meet the needs of the local communities in which they are chartered, consistent with safe and sound operations. The banking agencies' regulations implementing the CRA provide that the evaluation of a bank's CRA performance "is adversely affected" by evidence of discriminatory or other illegal credit practices "in any geography by the bank or in any assessment area by any affiliate whose loans have been considered as part of the bank's lending performance," as determined based on the regulator's discretion.

If you have any questions regarding the matters covered in this publication, please reach out to any of the lawyers listed below or your usual Davis Polk contact.

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