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Community Reinvestment Act and Its Impact on Bank Mergers

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I. INTRODUCTION

The United States Congress passed the Community Reinvestment Act (CRA or Act)[1] after neighborhood activists presented evidence that banks were withdrawing credit from minority neighborhoods while continuing to take deposits from them.[2] This banking practice directly contributed to the neighborhoods' deterioration. Community activists believed banks were engaging in "redlining," drawing red lines around certain inner-city, minority-populated areas, and refusing to make loans within those areas.[3] Tom Fox, director of San Diego based Normal Heights Community Development Corporation and one of the authors of the Act, stated that during his research in Chicago, a bank loan officer pulled a map out of a drawer and said he was not allowed to make loans in a neighborhood that had been clearly outlined in red.[4]

The initial impact of the Community Reinvestment Act on the regulation of financial institutions was not dramatic. For many years after its adoption in 1977, the CRA was little more than a vague statement of principle without much real-world effect.[5] In 1989, however, Congress greatly enhanced the CRA's impact as part of comprehensive banking legislation reform.[6] Currently, the role of the Act is expanding, and CRA-based challenges to bank mergers and other transactions subject to CRA scrutiny are now routine, even when the institution in question has received high marks for CRA compliance in recent examinations.[7] Some mergers and acquisitions

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1. Housing and Community Development Act of 1977, Pub. L. No. 95-128, § 801, 91 Stat. 1111, 1147-48 (1977) (codified as amended at 12 U.S.C. §§ 2901-07 (1994)).

2. *See* Alden Clark, *CRA: No Redlining*, BUS. J. CHAR., Dec. 21, 1987, at v2, n37.

3. *See id.*

4. *See id.*

5. *See* Paul H. Schieber, *A CRA Guide for Foreign Banks*, AM. BANKER, Feb. 14, 1992, at 6 (discussing, among other things, the actual effect of the CRA on banks).

6. Financial Institutions Reform, Recovery, and Enforcement Act of 1989, Pub. L. No. 101-73, § 1212, 103 Stat. 183, 526-28 (1989) (codified as amended at 12 U.S.C. §§ 2902, 2906 (1994)).

7. *See* John R. Wilke, *Home Loans to Blacks, Hispanics, Soared in '94*, WALL ST. J., July 19, 1995, at A1. The majority of the complaints were initiated by community activist organizations. These organizations expressed concern that the transactions would reduce, or even eliminate, needed services to minorities and to individuals of low- and moderate-

are actually derailed by the statute; however, even if the deals are not entirely defeated, the costs of consummating a transaction in the face of a CRA challenge can be substantial.[8]

As a result of its increasing impact on mergers and acquisitions, the CRA is now controversial. Many bankers, who want the scope of the CRA limited, argue that the statute imposes burdensome requirements and unfairly disadvantages depository institutions as compared to their nonbank competitors.[9] Community activists, who want to expand the Act's scope, contend that the CRA only begins to address problems of access to credit in low-income communities.[10] As traditional geographic and service restrictions on banking institutions continue to erode,[11] and as bank merger activity continues to increase, the Act's expanding impact on bank mergers may favor activists' interests. Consequently, in an attempt to shift the balance again, bankers have become more vocal in expressing their view that the CRA unfairly burdens their ability to create larger geographic

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income. They also argued that none of the banks against whom complaints were initiated were doing an adequate job of serving their communities under the CRA requirements. *See* Laura T. Beyer, Comment, *The Community Reinvestment Act: Boost to Low- and Moderate-Income Communities; Set-back for Minority-owned Banks*, 1 N.C. BANKING INST. 387, 394-95 (1997) (stating that only between one and two percent of applications filed with the Federal Reserve Board have been protested by community activist groups on CRA grounds since 1988).

8. *See* Ellen Braitman, *Fed Is Asked to Reconsider Blocking of Merger*, AM. BANKER, Nov. 25, 1991, at 5 (discussing First Interstate Bancsystem's requested reconsideration of the Federal Reserve Board's decision to turn down the bank's merger application).

9. *See* Jonathan R. Macey & Geoffrey P. Miller, *The Community Reinvestment Act: An Economic Analysis*, 79 VA. L. REV. 291, 312 (1993) (stating that the Act applies "only to depository institutions—banks and savings associations—and not to other types of lenders" and that "it discriminates within the category of depository institutions by placing greater disproportionate burdens on some institutions and thus giving an artificial competitive advantage to others").

10. *See Activists Think Mergers Will Aid Cause*, RECORD (Northern New Jersey), Sept. 15, 1995, at 4 (contending that banks ignore low-income neighborhoods in violation of the CRA).

11. In 1933, the McFadden Act amended the National Bank Act to permit national banks to establish and acquire branches within the state in which they were located to the same extent the state-chartered banks were permitted to establish and acquire branches. *See* McFadden Act, ch. 89, § 23, 48 Stat. 162, 189-90 (1933) (codified at 12 U.S.C. § 36 (1994)). The Douglas Amendment, section 3(d) of the Bank Holding Company Act, restricts acquisitions outside of the state where the acquirer's principal operations are conducted, except in such instances where the acquisition is specifically authorized by the laws of the state in which the acquired branch was located. 70 Stat. 133, 135 (1956) (codified at 12 U.S.C. § 1842(d)). A review of state banking laws published in 1989 indicated that most states have adopted some form of legislation permitting to some extent interstate acquisitions, with only three states continuing to prohibit interstate acquisitions entirely. Deborah A. DeMott, *Mergers and Acquisitions of Banks and Bank Holding Companies*, BANKING LAW AND REGULATION, 823, 829-831 (F. Puleo ed. 1990).

markets.

In light of this controversy, this Comment examines community reinvestment as a factor in the review of bank merger and acquisition requests. In doing so, this Comment (1) introduces the legislative history leading to the CRA,[12] (2) discusses the application of antitrust standards to banks,[13] (3) examines the evolution of "Community Reinvestment" in relation to antitrust standards,[14] and (4) identifies several shortcomings of the Act.[15] Ultimately, this Comment concludes that although the CRA has had only a mild impact on mergers and acquisitions in the past, the Act will become one of the most significant (if not controlling) factors in getting such deals approved in the future.[16]

II. LEGISLATIVE HISTORY

The debate preceding enactment of the CRA was similar to the current debate surrounding the Act. Community groups urged passage of the Act to curb what they believed to be a lack of adequate lending in low and moderate income areas.[17] On the other hand, bank and thrift officials generally opposed the CRA as an unnecessary measure that could, among other things, unduly affect business decisions by mandating credit allocation and cause safety and soundness problems by forcing institutions to make excessively risky loans.[18] However, legislators, activists, and bankers agreed that unless the practice of "redlining" low- and moderate-income communities ended, those communities could continue to deteriorate from a lack of financial resources.

Although concern about redlining was a prominent theme in the legislative history to the CRA, Congress did not perceive the proposed legislation as a means of directly prohibiting discrimination in lending.[19] Indeed, a leading community activist objected to the bill preceding the CRA specifically because the bill did not *expressly*

12. *See infra* notes 17-22 and accompanying text.

13. *See infra* notes 23-50 and accompanying text.

14. *See infra* notes 51-113 and accompanying text.

15. *See infra* notes 114-29 and accompanying text.

16. *See infra* notes 130-32 and accompanying text.

17. For further discussion, see *supra* note 2 and accompanying text.

18. *See generally* GEN. ACCT. OFF., COMMUNITY REINVESTMENT ACT: CHALLENGES REMAIN TO SUCCESSFULLY IMPLEMENT CRA (1995) (discussing some of the criticisms to the CRA offered by banks).

19. *See, e.g.*, 123 CONG. REC. 17,604 (1977) (statement of Sen. Proxmire).

"prohibit discrimination" in lending practices.[20] Despite activists' suggestions that Congress act firmly to prohibit such discrimination, Congress chose not to punish discrimination in lending in the CRA. Further, Congress did not envision the CRA as requiring affirmative action in lending on the basis of race, sex, ethnic background, or other categories. Additionally, Congress did not intend the CRA to induce depository institutions to support local charities or otherwise subsidize worthy causes. Instead, the overwhelming focus of the legislative history of the CRA was on the need to preserve local communities through a recognition of the fact that depository institutions could invest in their local communities and still make a profit.[21] Consequently, the CRA was phrased broadly to encompass depository institutions throughout the country, including institutions in suburban, rural, and wealthy urban areas as well as institutions serving decaying inner-city neighborhoods.

Ultimately, as the title of the statute indicates, the Act (and the legislative debates preceding the Act) focused on "communities" and reinvestment in those communities. The CRA responded to a concern about depository institutions transferring funds outside the communities in which the funds were obtained, regardless of whether those communities were rural, urban, or suburban. In other words, CRA emphasized communities, not race, ethnicity, gender, or other categories that dominate public policy debates in the 1990s.[22]

III. BANK MERGERS BEFORE THE CRA: ANTITRUST STANDARDS

Before the enactment of the CRA, approval of bank mergers was conditioned on satisfactory compliance with antitrust standards. Bank mergers, as a general matter, are subject to the same antitrust standards as mergers in other industries. However, when considered more closely, the antitrust analysis for bank mergers contains important differences from that analysis in other contexts. The development of the concept of "convenience and needs" in bank merger analysis accounts for most of these differences. This section of this Comment will explain the original view of federal regulations of bank mergers, explore the evolution of the original view of antitrust scrutiny of bank mergers, and discuss the implications of the

20. *See Community Credit Needs: Hearings on S. 406 Before the Senate Comm. on Banking, Housing, and Urban Affairs*, 95th Cong. 133 (1977).

21. *See, e.g.*, 123 CONG. REC. 17,631 (1977) (statement of Sen. Proxmire); *id.* at 17,633 (statement of Sen. Sarbanes).

22. Legislators both for and against the proposed statute agreed that the bill was aimed at bolstering decaying communities. *See id.* at 17,628 (statement of Sen. Morgan).

modern antitrust analysis of bank mergers and the relationship of this analysis to the CRA.

Bank merger activity was first regulated in 1956 when Congress enacted the Bank Holding Company Act (BHCA).[23] Congress intended the BHCA to prevent undue concentration of banking resources and to limit the geographic expansion of bank holding companies. Because the BHCA reached only mergers involving bank holding companies,[24] Congress passed the Bank Merger Act[25] in 1960. The Bank Merger Act expanded the scope of federal regulation of mergers to the entire banking industry. Because two pieces of specific legislation governed bank mergers, commentators thought that bank mergers were immune from scrutiny under the general antitrust standards of section 1 of the Sherman Antitrust Act of 1890[26] and section 7 of the Clayton Act.[27] This immunity, however, proved to be a fiction.

In *United States v. Philadelphia National Bank,*[28] the Supreme Court held that bank mergers were within the reach of section 7 of the Clayton Act.[29] In *Philadelphia National Bank*, the Office of the Comptroller of the Currency (OCC) approved the merger of two large Philadelphia banks.[30] The OCC granted this approval despite

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23. Bank Holding Company Act of 1956, Pub. L. No. 511, 70 Stat. 133 (1956) (codified as amended at 12 U.S.C. §§ 1841-1850 (1994)).

24. The BHCA specifically sets forth unlawful actions:

> [the BHCA makes it] unlawful, except with the prior approval of the [Federal Reserve] Board, (1) for any action to be taken that causes any company to become a bank holding company; (2) for any action to be taken that causes a bank to become a subsidiary of a bank holding company; (3) for any bank holding company to acquire direct or indirect ownership or control of any voting shares of any bank if, after such acquisition, such company will directly or indirectly own or control more than 5 per centum of the voting shares of such bank; (4) for any bank holding company or subsidiary thereof, other than a bank, to acquire all or substantially all of the assets of a bank; or (5) for any bank holding company to merge or consolidate with any other bank holding company.

12 U.S.C. § 1842(a) (1994).

25. Financial Deposit Insurance Act, Pub. L. No. 86-463, 74 Stat. 129 (1960) (codified as amended at 12 U.S.C. § 1828(c) (1994)) (amending the BHCA and expanding the scope of federal regulation of banking mergers).

26. Sherman Antitrust Act, ch. 647, § 1, 26 Stat. 209 (1890) (codified as amended at 15 U.S.C. § 1 (1994)). Section 1 of the Act prohibits contracts, combinations in the form of trust, and conspiracies in restraint of trade. *See id.*

27. Clayton Act, ch. 323, § 7, 38 Stat. 730, 731-32 (1914) (codified as amended at 15 U.S.C. § 18 (1994)). Section 7 of the Act prohibits monopolies that cause an unlawful restraint on trade and commerce. *Id.*

28. 374 U.S. 321 (1963).

29. *See id.* at 354.

30. *See id.* at 333

the fact that the Federal Reserve Board (FRB), the Federal Deposit Insurance Corporation (FDIC), and the Department of Justice found that the "proposed merger would have substantial anticompetitive effects."[31] In response to the banks' argument that the merger would stimulate economic development in the Philadelphia area, the Court held that a merger likely to lessen competition cannot be "saved because ... [of] some ultimate reckoning of social or economic debits and credits."[32] The Court stated that Congress' "value choice" to proscribe anticompetitive mergers reached benign and malignant mergers alike.[33]

In 1966, in response to *Philadelphia National Bank*, Congress passed amendments to the 1956 BHCA and to the Federal Deposit Insurance Act.[34] The 1966 amendments, like *Philadelphia National Bank*, recognized the right of the Department of Justice to challenge bank mergers on anticompetitive grounds.[35] On the other hand, unlike the holding of *Philadelphia National Bank*, the amendments provided that otherwise prohibited anticompetitive mergers could be lawful if their adverse competitive effects were clearly outweighed by their beneficial effects in meeting the "convenience and needs of the community."[36]

Portions of the principal statutory provisions that govern bank mergers and acquisitions[37] rely on the general statutory language of the Sherman and Clayton Acts.[38] However, these statutory provisions are fundamentally distinct from general antitrust laws because they

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31. *Id.* at 332-33.

32. *Id.* at 371.

33. *See id.*

34. *See* Bank Merger Act of 1966, Pub. L. No. 89-356, 80 Stat. 7 (1966) (amending the Federal Deposit Insurance Act and the BHCA).

35. *See id.*

36. The 1966 amendments to subsection (c) of section 3 of the BHCA revised the BHCA to provide that the Federal Reserve Board shall not approve

> any other proposed acquisition or merger or consolidation ... whose effect in any section of the country may be substantially to lessen competition, or to tend to create a monopoly, or which in any other manner would be in restraint of trade, unless it finds that the anticompetitive effects of the proposed transaction are clearly outweighed in the public interest by the probable effect of the transaction in meeting the convenience and needs of the community to be served.

Pub. L. No. 89-485,§ 7, 80 Stat. 236, 237-38 (1966).

37. *See* Change in Bank Control Act, 12 U.S.C. § 1817(j)(7) (1994); Bank Merger Act, 12 U.S.C. § 1825(c)(5) (1994); Bank Holding Company Act, 12 U.S.C. § 1842(c) (1994).

38. *See* 12 U.S.C. §§ 1817(j)(7)(A)-(B), 1828(c)(5)(A)-(B), 1842(c)(1)(A)-(B) (1994) (setting out general standards of the Sherman Act and the Clayton Act).

include "the convenience and needs of the community" defense.[39] While it is well established that bank regulators are required to apply general antitrust standards in evaluating the anticompetitive effects of proposed mergers, the analysis of competition is only part of the relevant inquiry.

In bank mergers and acquisitions, the responsible regulator must engage in a three-part evaluation.[40] The responsible regulator must engage in a competitive analysis,[41] a safety and soundness evaluation,[42] and a convenience and needs inquiry.[43] After the regulator delineates the relevant geographic and product markets,[44] the initial

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39. *See* 12 U.S.C. §§ 1817(j)(7)(B).

40. Determining which statutes control a merger or an acquisition and which regulatory agency reviews the transaction depends on the nature of the transaction and the charter of the acquiring or surviving bank and whether a bank holding company is a party to the proposed transaction. If the BHCA governs the transaction, approval by the Board of Governors of the Federal Reserve Board will be necessary. *See* 12 U.S.C. § 1842(a). If the transaction is governed by the Change in Bank Control Act, then approval must be obtained from the "appropriate Federal banking agency." 12 U.S.C. § 1813(q) (1994). The "appropriate agency" is (1) the Comptroller of the Currency in the case of a national banking association; (2) the Board of Governors of the Federal Reserve System in the case of a state-chartered bank that is a Federal Reserve member bank; (3) the Federal Deposit Insurance Corporation in the case of a state-chartered insured bank that is not a member of the Federal Reserve; and (4) the Office of Thrift Supervision in the case of a savings association or a savings and loan holding company. *See id.* If the transaction is governed by the Bank Merger Act, the "responsible agency" from whom approval must be given is (1) the Comptroller of the Currency if "the acquiring, assuming, or resulting bank is to be a national bank;" (2) the Board of Governors of the Federal Reserve System if "the acquiring, assuming, or resulting bank is to be a State member bank;" (3) the Federal Deposit Insurance Corporation if the "acquiring, assuming, or resulting bank is to be a State nonmember insured bank;" and (4) the Office of Thrift Supervision if the "acquiring, assuming, or resulting institution is to be a savings association." 12 U.S.C. § 1828(c)(2).

41. *See* 12 U.S.C. §§ 1817(j)(7)(A)-(B), 1828(c)(5)(A)-(B), 1842(c)(1)(A)-(B) (1994) (setting out general standards of the Sherman Act and the Clayton Act).

42. *See* 12 U.S.C. § 1817(j)(7)(C)-(F) (1994) (stating that the appropriate agency may disapprove any proposed acquisition if the financial condition of the acquiring bank might "jeopardize the financial stability of the bank or result in an adverse effect on the bank or savings association insurance fund"); 12 U.S.C. § 1828(c)(5) (1994) (stating that the "responsible agency shall take into consideration the financial and managerial resources and future prospects of the existing and proposed institutions"); 12 U.S.C. § 1842(c)(2) (1994) (stating that the Federal Reserve Board shall take into consideration the financial and managerial resources and future prospects of the companies and banks concerned).

43. *See* 12 U.S.C. §§ 1817(j)(7)(B), 1828(c)(5), 1842(c)(2) (1994) (stating that the appropriate regulator shall consider the convenience and needs of the community to be served).

44. The relevant geographic and product markets in which the merger will have a direct and immediate effect must be established to determine the probable competitive effects of a contemplated merger. "Product markets" derives from the phrase "line of commerce" in section 7 of the Clayton Act; "geographic markets" derives from the language "section of the country." *See* H. HOVENKAMP, ECONOMICS AND FEDERAL

competitive analysis evaluation requires the regulator to decide whether the proposed transaction will create a monopoly, further a combination or conspiracy to monopolize, or substantially lessen competition.[45] The second analysis, the safety and soundness evaluation, requires an assessment of the financial and managerial resources of the parties to the proposed transaction.[46] This analysis considers a number of factors, including the sources of capital for the transaction, the capitalization of the institutions involved, the competence and experience of management personnel, and the future prospects of the proposed and existing institutions. If the proposed merger is not precluded due to safety and soundness concerns, but is deemed to have significant anticompetitive effects, the regulator must then evaluate a third factor.[47] The third analysis balances the potential of the merger to enhance the "convenience and needs" of bank customers in the local community against the potentially anticompetitive effects of the transaction.[48] This convenience and needs inquiry requires the reckoning of social and economic debits and credits that was rejected in *Philadelphia National Bank.*[49]

Although antitrust standards are only one factor regulators analyze as they consider whether a proposed merger should be approved, the modern emphasis on the needs of local communities in this analysis parallels the interests of the CRA. Under the antitrust analysis, the responsible regulator must be satisfied that, after conducting a three-part test,[50] the benefits of meeting the "convenience and needs" of bank customers in the community outweigh the adverse competitive effect. Ultimately, this recognition of the importance of satisfying the banking needs of local communities was well entrenched in antitrust law prior to the enactment of the CRA.

IV. THE EVOLUTION OF "COMMUNITY REINVESTMENT"

In the late 1960s, banks seeking approval for mergers began to consider their ability to serve the "convenience and needs" of the

ANTITRUST LAW, § 3.3, at 62, § 3.5, at 70 (1985).

45. *See* 12 U.S.C. §§ 1817(j)(7)(A)-(B), 1828(c)(5)(A)-(B), 1842(c)(1)(A)-(B) (1994) (setting out general standards of the Sherman Act and the Clayton Act).

46. *See* 12 U.S.C. §§ 1817(j)(7)(C)-(F), 1828(c)(5), 1842(c)(2) (1994). For further discussion, see *supra* note 42 and accompanying text.

47. *See id.*

48. *See* 12 U.S.C. §§ 1817(j)(7)(B), 1828(c)(5), 1842(c)(2) (1994) (stating that the appropriate regulator shall consider the convenience and needs of the community to be served).

49. *See* United States v. Philadelphia Nat'l Bank, 374 U.S. 321, 323 (1963).

50. *See supra* notes 41-43 and accompanying text.

community in which they were chartered. Banks considered this factor because they could defend charges that their proposed merger violated antitrust laws by demonstrating that the merger enhanced their ability to effectively serve their communities. In the 1970s, Congress heightened the need for banks to focus on the "convenience and needs" of local communities when it passed the CRA. The CRA elevated the "convenience and needs" inquiry to an affirmative duty required for bank merger approval, rather than a defense to an allegation that the merger violated antitrust laws. As such, community needs and the CRA increasingly impact bank merger activity. Before one can recognize the growing impact of the CRA on bank mergers, one should understand the evolution of the Act over the last two decades. The history of the Act may be understood in three phases: (1) the original passage of the Act, (2) the amendments to the Act, and (3) the Act's evolving impact on bank mergers.

The Community Reinvestment Act was passed as Title VIII of the Housing and Community Development Act of 1977.[51] The CRA requires each federal banking regulator to encourage banks to meet the credit needs of the local communities in which they are chartered, consistent with the institution's safe and sound operation.[52] Consequently, regulators must assess an institution's record of lending in its community and take that record into account when evaluating an application by an institution for a merger or acquisition.[53]

Since the passage of the CRA, the regulatory, economic, and legislative environments, relative to the banking community, have changed. The CRA has been no exception. The Act has evolved significantly over the last two decades. Table 1 briefly illustrates the major amendments to the CRA since its passage.

In 1977, the CRA was enacted in response to a national concern over bank redlining[54] practices, and it highlighted Congress' concern that banking activity must recognize the "convenience and needs" of local communities. Although the Act uses the terms "convenience and needs," like the bank antitrust statutes, the Act creates an affirmative credit obligation rather than a potential defense to CRA violations. This affirmative duty is not enforced through direct civil

51. *See supra* notes 40-48 and accompanying text.

52. 12 U.S.C. § 2901 (1994).

53. *See* 12 U.S.C. § 2903 (1994).

54. Black's Law Dictionary defines "redlining" as a "pattern of discrimination in which financial institutions refuse to make mortgage loans, regardless of credit record of the applicant, on properties in specified areas because of alleged deteriorating conditions." BLACK'S LAW DICTIONARY 1279 (6th ed. 1990).

Table 1: Amendments to the CRA[55]

Year	Amendments
1977	Passed as Title VII of the Housing and Community Development Act of 1977.
1989	Amended by the Financial Institution Reform, Recovery, and Enforcement Act of 1989 (FIRREA) to require that CRA examination rating and a written evaluation of each assessment factor be made publicly available and to establish a four-part qualitative rating scale.
1991	Amended by the Federal Deposit Insurance Corporation Improvement Act of 1991 (FDICIA) to require public discussion of data underlying the regulator's assessment of an institution's CRA performance in the public portion of the CRA evaluation.
1992	Amended by the Housing and Community Development Act of 1992 to provide that the regulators consider activities and investments involving minority and women owned financial institutions and low-income credit unions in assessing the CRA performance records of institutions cooperating with such institutions to meet local community credit needs.
1994	Amended by the Riegle-Neal Interstate Banking and Branching Efficiency Act of 1994 to require that institutions with interstate branching structures receive a separate rating and written evaluation for each state in which they operate and a separate written evaluation of their performance within a multistate metropolitan area where they have branches in two or more states within the area.

or criminal penalties like other redlining statutes.[56] Instead, the CRA employs primarily indirect sanctions, including delays in or even denials of acquisition, merger, or branching requests.[57]

55. GEN. ACCT. OFF., COMMUNITY REINVESTMENT ACT: CHALLENGES REMAIN TO SUCCESSFULLY IMPLEMENT CRA (1995).

56. Attempts prior to the Community Reinvestment Act to control redlining practices included the Fair Housing Act of 1968, 42 U.S.C. §§ 3601-3631 (1994) (prohibiting discrimination on the basis of race, color, religion, or national origin in the financing of homes) and the Home Mortgage Disclosure Act. 12 U.S.C. §§ 2801-11 (1994) (requiring the collection and disclosure of lending records).

57. Financial regulatory agencies are required to take community reinvestment records into consideration in evaluating institutions' applications for deposit facilities. *See* 12 U.S.C. § 2903 (1994). An application for a "deposit facility" for purposes of the CRA

While the CRA has been criticized for its lack of effective enforcement mechanisms, the Act does empower each of the financial regulatory agencies to promulgate regulations[58] implementing Congress' mandate that "regulated financial institutions ... serve the convenience and needs of the communities in which they are chartered to do business."[59] Under this grant of authority, the financial regulatory agencies adopted regulations requiring banks to adopt and review the CRA policy statements [60] and to maintain a record of public comments on the bank's performance in meeting local credit needs.[61] The CRA also requires regulators to assess an institution's CRA performance under twelve "assessment factors," which focus upon the bank's community involvement.[62] On the basis of these assessment factors, regulators assign a CRA rating of "outstanding," "satisfactory," "needs to improve," or "substantial noncompliance."[63]

Amendments to the CRA contained in the Financial Institution Reform, Recovery, and Enforcement Act of 1989 (FIRREA)[64] require that the results of a CRA examination appear in "a written evaluation of the institution's record of meeting the credit needs of its entire community, including low- and moderate-income neighbor-

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includes requests for (1) charters; (2) deposit insurance; (3) branching approvals; (4) office relocations; and (5) mergers, consolidations, and acquisitions. *See* 12 U.S.C. § 2902(3) (1994).

58. *See* 12 U.S.C. § 2905 (1994). Regulations by the various financial supervisory agencies implementing the CRA are found in the Code of Federal Regulations. *See* 12 C.F.R. § 25 (1996) (regulations by the Comptroller of the Currency); 12 C.F.R. § 228 (1995) (regulations by the Federal Reserve System); 12 C.F.R. § 345 (1996) (regulations by the Federal Deposit Insurance Corporation); 12 C.F.R. § 563e (1996) (regulations by the Office of Thrift Supervision).

59. 12 U.S.C. § 2901(a)(1) (1994).

60. *See* 12 C.F.R. §§ 25.4, 228.4, 345.4, 563e.4 (1994).

61. *See* 12 C.F.R. §§ 25.5, 228.5, 345.5, 563e.5 (1994).

62. *See* 12 C.F.R. §§ 25.7, 228.7, 345.7, 563e.7 (1994). The assessment factors included: (1) the activities of the bank to ascertain credit needs of its community; (2) the bank's marketing practices; (3) the participation of the board of directors in formulating and reviewing CRA policies; (4) practices by the bank that discourage particular types of credit applications; (5) the bank's geographic distribution of credit; (6) evidence that the bank has engaged in illegal practices; (7) the opening and closing of bank offices; (8) involvement of the bank in development and redevelopment projects; (9) home mortgage, small business, and small farm loans by the bank; (10) the bank's participation in government-issued loan programs; (11) the bank's resources in meeting community credit needs; and (12) other factors which reasonably bear on the extent to which a bank is meeting credit needs. *See id.*

63. 12 U.S.C. § 2906(b)(2) (1994).

64. Pub. L. No. 101-73, § 1212(b), 103 Stat. 183, 527-28 (1989) (codified at 12 U.S.C. § 2906 (1994)) (amending the Community Reinvestment Act to require, beginning July 1, 1990, disclosure of the public section of an examining agency's CRA evaluation of an institution).

hoods."[65] The written evaluation must contain both a public and a confidential section.[66] The public section must be made available to the public for any CRA examination conducted on or after July 1, 1990.[67]

Despite the original purpose of the Act to encourage banks to meet the credit needs of the local communities in which they are chartered, and despite the original amendments intended to provide an enforcement mechanism for the Act, few branching or merger requests have been denied on CRA grounds.[68] This is unlikely to continue.[69] In 1995, Congress issued sweeping new changes to the CRA,[70] and future regulations are on the horizon. These amendments serve to increase the effectiveness of the CRA.

In 1995, concerns about the effectiveness of the CRA and its regulatory burden on institutions led both the Clinton administration and Congress to seek new methods to make the CRA more effective and less burdensome.[71] The stated goals of the regulators' reform initiative, announced by President Clinton in July 1993, were to (1) base CRA examinations more on results than paperwork, (2) clarify performance standards, (3) make examinations more consistent, (4) improve enforcement to provide more effective sanctions, and (5) reduce the costs and burdens of compliance.[72] Subsequently, regulators issued two notices of proposed rule making.[73] The first notice was issued by the FRB, OCC, Office of Thrift Supervision (OTS), and FDIC on December 21, 1993.[74] The proposal would have replaced the current qualitative CRA examination system, including the twelve assessment factors, with a more quantitative system based on actual performance as measured through the use of three tests:

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65. 12 U.S.C. § 2906(a)(1) (1994).

66. *See* 12 U.S.C. § 2906(a)(2) (1994).

67. *See* 12 U.S.C. § 2906(b) (1994).

68. *See* Beyer, *supra* note 7, at 394-95 (stating that only between one and two percent of applications filed with the Fed have been protested by community activist groups on CRA grounds since 1988).

69. *See id.* at 399-400 (discussing the recent trend of the Federal Reserve Board to approve large bank mergers, but stating that over 50 percent of the merger transactions approved by federal regulators during the fourth quarter of 1996 were contested and that a large number of the protests were filed under the Act).

70. Community Reinvestment Act Regulations, 60 Fed. Reg. 22,156 (1995) (to be codified at 12 C.F.R. §§ 25, 228, 563e, 203, 345).

71. *See id.*

72. *See id.*

73. *See supra* note 18.

74. *See* Community Reinvestment Act Regulations, 58 Fed. Reg. 67,466, 67,467 (1993) (proposed Dec. 21, 1993).

the lending, service, and investment tests.[75] Regulators released the second proposal via publication in the Federal Register on October 7, 1994.[76] This proposal revised the original proposal and increased the role of examiner discretion in CRA examinations. After receiving extensive public comments, regulators promulgated the revised CRA regulation in May 1995.[77]

The new CRA regulation, like past regulations, applies to all insured banks and thrifts engaged in lending to the public. It adopted the three part, performance-based, evaluation system for institutions that do not qualify as small institutions.[78] The regulation defines small institutions as independent retail institutions with total assets of less than $250 million and holding company affiliates with total assets of less than $1 billion. The revised regulation includes a streamlined examination for small banks and the option for all institutions to have their CRA performance examined according to a regulator-approved strategic plan.

Recognizing the diversity in communities' characteristics and needs, the revised CRA regulation makes explicit the "performance context" against which the tests and standards set out in the proposed regulation are to be applied. This "performance context" includes consideration of six factors concerning the unique characteristics of the institution under examination and the market in which it operates.[79]

The data collection provisions of the new regulation became effective on January 1, 1996. The new CRA standards themselves, however, will not become effective until July 1, 1997. Small institu-

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75. *See id.*

76. *See* Community Reinvestment Act Regulations, 59 Fed. Reg. 51,232, 51,234 (1994) (proposed Oct. 7, 1994) (discussing comments on the market share component and reasons for modifying the Lending Test).

77. *See* Community Reinvestment Act Regulations, 60 Fed. Reg. 22,156.

78. Specifically, (1) the lending test is designed to measure a retail institution's performance in meeting the credit needs of its assessment area, as measured by originations and purchases of home mortgages, small business and small farm loans, and community development loans; (2) the investment test considers the institution's record of helping to meet the credit needs of its assessment area (the test includes only investments that benefit the institution's assessment area or areas, or benefit a larger region that includes those areas) through qualified investments; and (3) the service test evaluates an institution's record of helping to meet the credit needs of its assessment area or areas by evaluating: (i) the availability and effectiveness of the institution's retail delivery systems; and (ii) the extent and innovation quality of its community development services. *See Community Reinvestment and Home Mortgage Disclosure (FRB Regulations BB and C)*, COMPLIANCE ALERT, June 12, 1995 [hereinafter *Home Mortgage Disclosure*]. For further discussion, see *supra* note 70 and accompanying text.

79. *See supra* note 18.

tions automatically came under the small-institution rules as of January 1, 1996, unless they chose to comply with the lending, investment, and service tests. Institutions must submit strategic plans by April 1, 1997, in order to be qualified by the time the rule goes into full effect.[80]

Because the new CRA revisions emphasize performance, not process, banks will be able to focus more on lending and less on paperwork.[81] Arguably, this should push banks even further into low- to moderate-income communities.[82]

As the 1995 amendments become fully effective this year, lawmakers are continuing to work on additional changes to the CRA for the future. Unlike current revisions to the CRA, which strengthen the enforcement provisions and make CRA compliance a more significant consideration for banks seeking mergers, proposed changes to the Act appear to focus more on streamlining the application process for mergers and acquisitions. The Board of Governors of the Federal Reserve System has proposed a comprehensive amendment to the BHCA and Change in Bank Control Act, known as Regulation Y.[83] The proposed amendment is intended to improve the competitiveness of bank holding companies by eliminating unnecessary regulatory burdens and operating restrictions and by streamlining the application/notice process.[84] The Board also proposed to establish a streamlined and expedited review process for bank and nonbanking proposals by well-run bank holding companies.

Two important principles underlie these proposed revisions. First, the new regulation would establish objective and verifiable measures for each of the criteria set forth in the BHCA.[85] In addition, these new regulations would provide an expedited and nearly red-tape-free merger approval process for those bank holding companies that meet stated measures. Second, the application/notice

80. *See Home Mortgage Disclosure, supra* note 78.

81. *See* Beyer, *supra* note 7, at 394.

82. *See id* at 397-98.

83. Bank Holding Companies and Change in Bank Control (Regulation Y); Proposed Rule, 61 Fed. Reg. 47,242 (1996) (to be codified at 12 C.F.R. § 225).

84. *See id.* The proposal would permit a well-rated and well-run BHC to acquire banks and nonbanking companies and to engage in permissible nonbanking activities de novo with the filing of a simple short letter and only 15 days advance notice. All bank acquisition proposals that exceed 35 percent of assets (or cause a small BHC to exceed $300 million in assets) or that involve bank holding companies that otherwise do not meet the qualifying criteria would be reviewed under the FRB's current 30/60-day procedure. *See id.* at 47,243.

85. *See id.*

process, according to the proposed revisions, would focus on an analysis of the effects of the specific merger proposal and should not normally become a vehicle for comprehensively evaluating and addressing CRA supervisory and compliance issues.[86]

This amendment to the BHCA has met with heavy resistance from community activists groups. These groups believe that the fifteen-day streamlined notice period would not allow adequate time for concerned organizations to file formal comments opposing a merger or acquisition.[87] Community activist groups view the proposal as a way of limiting the effectiveness of the CRA. However, banks seeking approval for mergers or acquisitions view the proposed regulation as an efficient method for consummating the transaction.

As a result of the revised CRA, which effectively reduces "paperwork compliance" with the Act and places more emphasis on performance, and the proposed Regulation Y, which expedites the approval process for bank mergers and acquisitions, banking customers in low- and moderate-income communities should see a resurgence of banking activity in their areas. This resurgence will be a consequence of the reduced cost of compliance with the CRA and the increased enforcement provided by the revised Act.

As a result of amendments enhancing enforcement, and of proposed amendments streamlining banks' ability to assure compliance with CRA, the CRA's impact on the banking industry should grow rapidly.[88] In recent years, several branching, merger, and conversion requests have been delayed on CRA grounds.[89] The increased focus of regulators on the CRA, evidenced by the 1989 joint CRA statement, the FIRREA amendments to the CRA, and the success community groups have experienced in challenging merger and acquisition applications on CRA grounds all indicate that this trend will continue.[90]

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86. *See id.*

87. The new procedure provides, however, that the Federal Reserve System's (System) action is subject to revocation if the primary supervisor (FRB, FDIC, OCC, or OTS) objects to a transaction within the relevant notice period. Because bank acquisition proposals may not be consummated for 15 days after System's action, which is the post-approval waiting period established by statute to allow the Department of Justice to review a transaction, it is expected that the notice period for the primary supervisor will expire prior to consummation of a bank acquisition proposal. *See id.*

88. *See id.*

89. *See Mitsui Bank Withdraws Application for Conversion of Nonbank Trust Unit*, 57 Banking Rep. (BNA), at 169, 173 (1991) (stating that Tokyo's Mitsui Taiyo Kobe Bank withdrew its request to convert Taiyo Kobe Bank and Trust Co. in New York City to a commercial bank, arguably out of concern for denial of the request on CRA grounds).

90. *See CRA Hurdles Get Higher*, BANK EXPANSION REPORTER, Sept. 19, 1988, at 4-

Compliance with the CRA is gradually shifting from being a relevant factor in the assessment of a proposed transaction's non-competitive effects toward being a controlling factor. The substantial attention regulators give to an acquiring institution's CRA record reflects a regulatory belief that "financial institutions that make meeting their responsibilities under the CRA an integral part of their management and operational structure are best able to accomplish the goals of the statute which includes meeting the credit needs of their entire communities, including low- and moderate-income neighborhoods, consistent with safe and sound operations."[91]

Most CRA-related challenges do not result in the denial of a merger application.[92] Instead, the acquiring institution and the protesting community group, or responsible regulatory agency, usually reach a settlement.[93] Though the forms of settlements may vary substantially, institutions are usually required to make substantial CRA commitments.[94] In effect, these "CRA commitments" are typically loan commitments for a specific dollar amount.[95] The CRA commitments generally win regulator approval for a transaction;[96] however, that is not always the case.

For example, the FRB denied Continental Illinois Bancorp's application to acquire an Arizona bank, despite Continental's proposal to remedy its CRA deficiencies via loan commitments.[97] Continental applied to the Fed under section 3 of the BHCA to acquire all the voting shares of Grand Canyon State Bank, a small state-chartered commercial bank.[98] The competitive effects of the merger were not at issue. The Fed's analysis instead focused on the needs of the community to be served by Continental's present and proposed bank subsidiaries. The order issued by the Fed stated that while CRA improvement commitments are often sufficient to secure approval,

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6 (summarizing Federal Reserve Board decisions addressing CRA issues).

91. *See Crestar Financial Corp.*, 75 Fed. Res. Bull. 382 (1989); *see also Core States Financial Corp.*, 76 Fed. Res. Bull. 176, 178-79 (1990).

92. *See* Beyer, *supra* note 7, at 400.

93. *See* Ellen Braitman & Yvette Kantrow, *NCNB and C&S Make $10 Billion CRA Pledge*, AM. BANKER, Aug. 7, 1991, at 1 (discussing two major bank holding companies' agreements to extend ten billion dollars in "community development" loans over a ten year period after political activists announced their intention to file CRA challenges to their proposed combination).

94. *See id.*

95. *See id.*

96. *See FED Rules Illinois Thrift May Form Bank Holding Company Despite CRA Violations*, 47 Wash. Fin. Rep. (BNA), Oct. 27, 1986, at 699.

97. *Continental Illinois Bancorp, Inc.*, 75 Fed. Res. Bull. 304 (1989).

98. *Id.*

merger approval would be withheld where the acquiring institution failed to establish a record indicating "a basic level of compliance on which the commitments can be evaluated."[99] The Continental order could guide future decisions of the Fed in light of statistics compiled by federal bank regulators indicating that nearly one out of every ten financial institutions examined with respect to CRA compliance since July 1, 1990, received a less-than-satisfactory CRA rating.[100]

In addition to the Continental order, the Federal Reserve Board blocked a proposed merger between First Interstate Bancsystem of Montana, Inc., based in Billings, Montana, and Commerce Bancshares of Wyoming, Inc., based in Sheridan, Wyoming.[101] The denial followed a protest by Native Action, a community group located on the Northern Cheyenne Indian Reservation, alleging that a subsidiary bank of First Interstate had failed to take steps to address and meet the credit needs of the reservation community. The Fed agreed with the Native Action's allegations, recognizing that First Interstate had little contact with the reservation.[102] The Board also noted two "less-than-satisfactory" CRA ratings by the FDIC.[103] The Board indicated that while the bank had made some Small Business Administration and other loans in its community, it had made only a limited number of loans to members of the reservation and had taken action to improve its CRA performance only after the merger application had been filed.[104] As in Continental, no competitive issues were raised and the denial of merger approval was based solely on community reinvestment grounds.

At this point in the evolution of community reinvestment, the Continental and First Interstate orders still represent isolated circumstances in which bank merger or acquisition applications were denied solely on CRA grounds.[105] However, delays in the merger approval process resulting from community group CRA challenges have already become more commonplace.[106] For example, the Charlotte Reinvestment Alliance's (the Alliance) effort to block NCNB Corp.'s (now NationsBank) acquisition of two Tampa-area branches

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99. *Id.* at 306.

100. *See supra* note 18.

101. *Fed Blocks Attempted BHC Merger, Cites CRA Concerns by Cheyenne Group*, 57 Banking Rep. (BNA) No. 15, 1991, at 587, 603.

102. *Id.*

103. *Id.*

104. *Id.*

105. *See* Beyer, *supra* note 7, at 394 n.58.

106. *See id.* at 399-400.

of Florida's American Savings & Loan resulted in extensive delays in getting regulatory approval for the acquisition. The Alliance claimed, based on a study of mortgage lending in minority areas in Charlotte, that NCNB "had done very little in the way of community reinvestment."[107] The Alliance, successful in negotiating $9 million in CRA commitments from First Union Corp. as a result of a 1989 merger, was joined by community groups in Texas who filed complaints alleging that NCNB failed to meet its CRA obligations in minority areas in Austin, Dallas, Houston, and San Antonio.[108] First Union's application to acquire Florida National was also delayed on CRA grounds. In commenting on its decision to approve First Union's bid, the Federal Reserve Board noted that "if not for the deteriorating condition of Florida National ... it would not have approved ... [the] bid ... [in light of First Union's] past CRA performance."[109] Within days of the announcement that a merger agreement had been reached between NCNB Corp. and C&S/Sovran Corp., it was announced, apparently as part of an effort to stave off CRA challenges, that $10 billion would be committed to community development lending in existing NCNB and C&S/Sovran markets over the next ten years.[110] Shortly after the announcement, the Federal Reserve Board announced that it would conduct four public hearings in connection with NCNB's application to acquire C&S/Sovran.[111]

While post-Continental Board orders suggest that CRA is not the beginning of the end of the convenience and needs inquiry,[112] Continental and First Interstate do indicate that a basic level of compliance could, as a matter of course, be a necessary condition for the approval of a merger or branching request.[113] An established record of CRA compliance would, most certainly, provide a more objective basis for determining whether a merger or acquisition is likely to have the probable effect of meeting the convenience and needs of the

107. *Community Groups Protest NCNB's Record Under CRA in Florida, Texas*, 55 Banking Rep. (BNA) No. 15, 1990, at 605, 613.

108. *See id.*

109. *Fed OKs First Union Acquisition, Sets Tough CRA Compliance Conditions*, 54 Banking Rep. (BNA) No. 1, 1990, at 1, 10.

110. *See* Martha Brannigan, *NCNB, C&S Sovran Plan to Expand Lending for Community Development*, WALL ST. J., Aug. 7, 1991, at A5.

111. *See Fed to Hold Public Hearings in Four Cities in NCNB-C&S Sovran Merger Plan*, 57 Banking Rep. (BNA) No. 12, 1991, at 441, 448.

112. *See First Union Corporation*, 76 Fed. Res. Bull. 83, 87 (1989).

113. Richard Ringer, *Memphis Thrift Denied Branch on CRA Grounds*, AM. BANKER, July 24, 1989, at 3.

community than would a commitment for future action.

V. COMMUNITY REINVESTMENT ACT: ITS NEGATIVE IMPACT

As the impact of the CRA continues to grow, commentators have begun to look closely at the potentially negative effects of this reality. Since its enactment in 1977, members of the banking industry have criticized the CRA. Specifically, bankers have noted three adverse effects of the CRA on the banking industry: (1) the Act creates a competitive disadvantage; (2) the Act provides tools for political activists; and (3) the Act introduces a deterrent to investment.

A. Competitive Disadvantage

Bankers suggest that the CRA discriminates on two levels. First, the CRA subjects the banking industry to costs and burdens that are not imposed on similarly situated lending institutions. Consequently, the Act places depository institutions at a competitive disadvantage compared with their nonbank competitors. Second, within the depository institution industry, the CRA discriminates against wholesale banks and other specialized institutions that are not well-adapted to community investment lending.

The CRA imposes significant compliance costs on institutions, especially smaller institutions.[114] It induces socially unproductive expenditures on public relations and documentation that provide no benefit for local communities.[115] Furthermore, its requirements are vague and self-contradictory, and its enforcement often appears arbitrary.[116] Nevertheless, depository institutions, unlike other similarly situated institutions, must incur the costs necessary to satisfy the requirements of the CRA.

B. A Tool for Activists

Just as bankers criticize the CRA because it allegedly creates a competitive disadvantage, bankers criticize the Act as simply creating a tool for political activists. Bankers contend that activists use the

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114. *See "Mindless" Regulations Attacked*, AM. BANKER, July 6, 1992, at 7 (stating that one small institution in rural Nebraska, with only $16 million in assets, reportedly was subjected to a week-long CRA exam by six examiners).

115. *See* Barbara A. Rehm, *ABA: Cost of Compliance Equals 59% of Bank Profits*, AM. BANKER, June 18, 1992, at 1, 12 (stating that a study compiled by the American Bankers Association in 1992 concluded that the banking industry spent $10.7 billion complying with government regulation in 1991, and that the single most costly regulation of all was the CRA).

116. *See id.*

CRA to accomplish goals that the act was not intended to serve, and for which it was poorly designed.[117] The statute encourages banks to engage in affirmative action in hiring and credit allocation,[118] and the Act is administered to encourage charitable giving by depository institutions.[119] Regardless of the social benefits of affirmative action or charitable giving, the CRA was not designed to serve these goals. Using the Act to further these goals represents a distortion of its original purpose.

More specifically, the CRA has become a potent political tool in the hands of activist political groups. Activists have used the statute to magnify their political importance, to gain special favors for themselves and their leaders, to obtain funding for pet projects, or garner direct logistical or financial support for their operations.[120] Essentially, some political leaders use the threat of a CRA challenge for self-serving purposes rather than to serve the purposes of the Act. This reality should not call into question the motives of all activist groups, the great majority of which are reputable and public-spirited,[121] but it should suggest that activist groups, like the rest of

117. *See* Jim Salter, *Protest planned for NationsBank merger,* NEWS & OBSERVER, Nov. 23, 1996, at 8D (describing the actions of a group, led by University City, Missouri lawyer Eric Vickers, that protested the merger of NationsBank and Boatmen's Bancshares and that asked NationsBank officials to, among other things, agree to add two African-Americans to NationsBank's board of directors); *see also,* Kenneth Cline, *NAACP to Push for Hiring of More Blacks,* AM. BANKER, Dec. 10, 1990, at 1 (stating that the NAACP threatened CRA challenges to institutions that did not hire more African-American employees).

118. *See* Cline, *supra* note 117, at 1, 6 (explaining that civil rights groups will ask banks to agree to hire more blacks as condition to the groups dropping their CRA protests).

119. *See* Teresa Carson, *Wells Takes the Cultural Route,* AM. BANKER, Jan. 13, 1992, at 10 (stating that Wells Fargo donated a landmark Victorian house in downtown Sacramento, valued at $1 million, to a group promoting Chicano art with the explicit purpose of earning CRA points with the regulators).

120. *See* Joel B. Obermayer, *First Citizens answers critics with initiative,* NEWS & OBSERVER, Oct. 16. 1996, at 7A (noting that First Citizens accused Community Reinvestment Association of North Carolina (CRANC) of trying to extort $750,000 for its own benefit and that CRANC officials replied that they had only proposed that First Citizens give $150,000 a year over five years to community groups and nonprofit organization in North Carolina to hire counselors who would be able to help people apply for loans).

121. *See* Letter from Irvin Henderson, President, Community Reinvestment Association of North Carolina, to Carla Holiman, Applications Analyst, Office of Thrift Supervision Department of the Treasury (June 11, 1996). In the letter, Mr. Henderson noted that:

> In both of its last two evaluations of First Citizens' community reinvestment performance in North Carolina, the FDIC cited the Bank for numerous violations of the Fair Housing Act, Home Mortgage Disclosure Act and Equal Credit Opportunity Act. These violations were of a serious enough nature to prompt James B. Hyler, Vice-Chairman of First Citizens, to send all Bank personnel a memo

society, respond to incentives in order to serve their own interests.

Bankers assert that rather than manipulating the CRA to serve purposes for which it was not designed, activists should use alternative methods to accomplish their goals. For example, local organizations could work at the grass roots level to raise capital and extend credit to community members who are known to the organization and whose credit-worthiness can be monitored. However, the CRA does not require subsidizing poor or disadvantaged citizens. Consequently, that goal could more adequately be served by direct subsidy programs rather than by treating depository institutions as some form of public utility that can be assessed to serve general social needs.

C. A Deterrent to Investment

Commentators allege that the CRA "poorly furthers the purposes for which it was designed."[122] It penalizes institutions that actually serve low- income and moderate-income neighborhoods, while rewarding those that do not. In other words, the Act drives capital away from poor neighborhoods by imposing a tax on those depository institutions reckless enough to do business in such communities,[123] discourages innovation in the provision of financial services to low- and moderate-income neighborhoods, and might impair the market position of existing institutions that serve local community needs.

The CRA has different effects on varying types of depository institutions.[124] These differing effects manifest themselves in a variety of ways. First, the Act discriminates against depository institutions serving poor neighborhoods. Because a bank's CRA rating is based on its lending practices in the area contiguous to its offices, the CRA imposes greater costs on banks in poor areas than those in wealthy areas to the extent that it causes banks to lend funds locally.[125] Banks

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> which stated that if changes were not made, "the matter could be turned over to the Department of Justice, which could very well bring aspects of our business to a halt."

Id. (quoting NEWS & OBSERVER, Oct. 29, 1995). *But see* Joel Obermayer, *First Citizens answers critics with initiative*, NEWS & OBSERVER, Oct. 16, 1996, at 1A (noting that in response to the Community Reinvestment Association of North Carolina (CRANC) attempt to block First Citizens' $7 billion expansion into Georgia, the bank accused CRANC of trying to extort $750,000 for it own benefit).

122. Macey & Miller, *supra* note 9, at 296.

123. *See* Ray G. Huffaker, *Market-Based Policies to Increase Home Mortgage Credit in Declining Urban Neighborhoods*, 106 BANKING L.J. 538, 541-46 (1989).

124. *See id.*

125. This analysis assumes that it costs more to make loans in poor areas than in

located in wealthy areas can elect not to make loans in poor areas outside their immediate communities without risking serious CRA challenges. Banks located in poor areas, on the other hand, are required by the CRA to devote a substantial proportion of their loan portfolios to their local communities.[126] Because of these additional regulatory requirements and costs, banks seeking to expand may be less likely to establish new branches or offices in poor areas than they were prior to the promulgation of the CRA.

Additionally, some institutions might close offices in certain neighborhoods because they could be publicly criticized for not meeting the credit needs of such neighborhoods when they attempt to acquire a branch in another location.[127] This closure of offices would increase the present concentration of financial institution offices in more affluent neighborhoods.[128]

Ultimately, as the role of the CRA continues to expand, bankers will continue to criticize the Act's negative effects. This open criticism should draw attention to concerns about the competitive disadvantages the Act imposes on the banking industry, the potent tool the Act has become in the hands of political activists, and the deterrent to investment created by the Act. As legislators receive information about these adverse effects of the Act, future legislation may address these problems.[129]

VII. CONCLUSION

The evolution of the Community Reinvestment Act from a prohibition on redlining to an affirmative local credit obligation required to win approval of mergers and acquisitions has drawn considerable

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wealthy areas.

126. *See* 12 U.S.C §§ 2901(a)(1), (3). The CRA begins with the recitation that "regulated financial institutions are required by law to demonstrate that their deposit facilities serve the 'convenience and needs' of the communities in which they are chartered to do business," and that "regulated financial institutions have [a] continuing and affirmative obligation to help meet the credit needs of the local communities in which they are chartered." *Id.*

127. *See* Letter from Robert E. Barnett, Chairman, FDIC, to Senator William Proxmire (May 4, 1977). Mr. Barnett wrote that the CRA would have the effect of reducing the availability of credit in impoverished areas was well understood at the time the statute was enacted. Mr. Barnett, then Chairman of the FDIC, objected to the legislation on exactly those grounds at that time. He argued persuasively that the practical effect of the bill might be to discourage financial institutions from making applications for offices in neighborhoods where funds are badly needed because of the reexamination that this would entail with respect to their lending policies in service areas where they already had offices. *See id.*

128. *See id.*

129. For a discussion of regulation Y, see *supra* note 83 and accompanying text.

attention in the banking industry. Since its enactment in 1977, the CRA has generated intense and often bitter controversy. While all participants in the debate continually claim allegiance to the goals of the Act, disagreement over the extent to which the Act should intervene into the affairs of regulated institutions has stalled efforts to revitalize and strengthen our communities.

A review of the legislative history of the CRA reveals significant debate prior to its enactment. The community activists supported the enactment of the CRA, which they hoped would increase lending in low- and moderate-income communities. The banking industry, on the other hand, was concerned that the CRA would unduly burden the ability of banks to make sound business decisions. Ultimately, through its evolution and subsequent revisions, the CRA addresses the concerns of both community activists and the banking industry by emphasizing reinvestment and less burdensome regulatory requirements. The revised Act provides financial institutions with more objective criteria to assess their CRA performance.[130] Further, the proposed amendment to the CRA should streamline the merger application process, resulting in increased banking activity in low- and moderate-income areas.

Community groups will also benefit from the revised Act. By encouraging public input, the agencies have acknowledged the importance of local community groups in the CRA process.[131] Banks, instead of seeing community groups as their opponents in a merger or acquisition, will be more apt to solicit information from community activist groups to lessen their compliance costs. In addition, because community groups make it a practice to be more informed about the credit needs of their specific community, banks have added incentive to work closely with community groups in order to reduce their research costs[132] as banks seek to satisfy the "convenience and needs" requirements of antitrust statutes and the CRA.

With a new wave of bank and thrift mergers and acquisitions on

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130. *See* Community Reinvestment Act Regulations, 60 Fed. Reg. 22,156. Because the CRA does not mandate credit allocation, there must be room for some agency discretion. However, the new regulations balance this need with the need for more objectivity in the examination process. *See id.*

131. *See id.*

132. *See* Claudia Cummins, *Texas Commerce Puts Teamwork Into CRA*, AM. BANKER, Sept. 9, 1993, at 18 ("[Bankers] need to access the expertise that already exists in community lending, redevelopment, and affordable housing, and find partners that know how to get the dollars into the community." (statement of Marc Shapiro, President and Chief Executive Officer of Texas Commerce Bancshares) (internal quotation marks omitted)).

the horizon, the role of the Community Reinvestment Act will continue to increase. As the CRA assumes a more prominent position in the merger and acquisition approval analysis, the CRA will strengthen the antitrust considerations in this approval process. In fact, if current trends continue, the CRA may become the sole standard for determining whether an acquiring institution has a "convenience and needs" defense to an otherwise prohibited merger. Perhaps more importantly, however, as the level of community involvement in banking decisions continues to increase, a CRA record could become the sole basis for decisions with respect to branching and merger and acquisitions requests.

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