June 17, 2004

Jennifer J. Johnson
Secretary
Board of Governors of the Federal Reserve System
20$^{th}$ & Constitution Avenue, N.W.
Washington, DC 20551-0001

Dear Ms. Johnson,

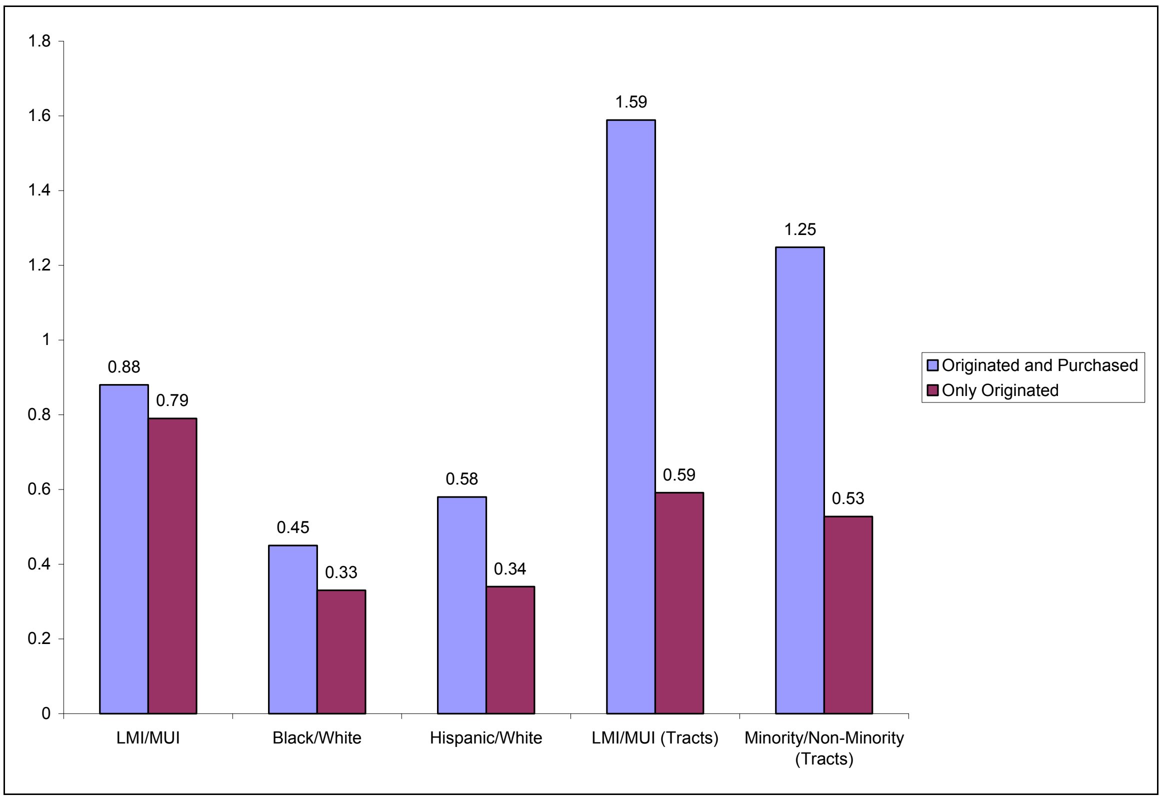
I am writing from the Woodstock Institute in Chicago to comment on the proposed acquisition of Charter One Bank by Citizens Financial Group, a subsidiary of Royal Bank of Scotland. Woodstock Institute is a Chicago-based research and policy organization that for over 30 years has worked locally and nationally to promote reinvestment in lower-income and minority communities. Woodstock Institute also convenes the Chicago CRA Coalition, a group of nearly 100 area organizations with an interest in increasing access to financial services in underserved communities. For the past five years, the Coalition has had a Community Reinvestment Agreement with Charter One Bank. This agreement sets specific goals for the bank to meet in areas such as mortgage lending, branch distribution, and levels of grants and investments. Over the course if the agreement, the bank has made significant progress towards meeting many of these goals, but we still have concerns about aspects of Charter One's performance.

We commend Charter One for regularly meeting grants and investments goals; conducting numerous financial literacy training events; increasing levels of lending to smaller multifamily properties in lower-income and minority communities; and improving its branch presence in underserved areas. We also recognize the bank's efforts to offer new account products appropriate for low-income people and provide an outstanding level of marketing and outreach in this area.

However, we continue have concerns about the bank's distribution of mortgages to minority borrowers and to low- and moderate-income (LMI) and minority census tracts. Additionally, we are troubled by the bank's heavy reliance on purchased, as opposed to directly originate, loans in underserved areas.

An analysis Charter One's 2002 Chicago area mortgage lending shows that the bank tends to have a larger share of middle- and upper-income (MUI) and white mortgage markets than LMI and minority markets. Charter One is a significant lender in the Chicago area, ranking ninth for single-family mortgages. Examining home purchase lending, Chart 1 shows that, when considering both directly originated and purchased loans, the bank's market share ratios (MSR)[1] are below 1.0 when looking at borrower characteristics. We are particularly troubled by the bank's inability to lend to minority borrowers. For example, in 2002 Charter One's African American/White MSR was .45 and their Hispanic/White MSR was .58. Both of these numbers are well below 1.0, indicating that Charter One tends to target lending to white borrowers much more heavily than to minorities.[2]

**Chart 1.** Charter One Chicago Area Home Purchase Lending Market Share Ratios With and Without Purchased Loans, 2002




In addition to problematic lending to minorities, we are concerned that Charter One Bank relies heavily on purchased loans to meet CRA and other lending goals. For example, Table 1 shows that, in 2002, 43 percent of Charter One's home purchase loans to Hispanics and 29 percent of home purchase loans to African Americans were purchased as opposed to directly originated. If we consider only loans directly originated, Chart 1 shows that Charter One's MSRs comparing lending to minority and white borrowers drop significantly. The use of purchased loans is particularly

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[1] Market share ratio analysis compares a bank's presence (market share) in comparable, discreet markets (i.e. LMI-MUI). An ideal market share ratio is 1.0 indicating that a bank has an equal presence in both markets. A number well above or below 1.0 indicates a lender disproportionately targets or ignores one market.

[2] A significant share of Charter One's purchased loans have no information on borrower characteristics. Because of this, the market share ratios by borrower characteristic differ significantly from those by tract characteristic when purchased loans are included.

problematic in LMI and minority communities. In 2002, 63 percent of home purchase loans to LMI census tracts and 60 percent of home purchase loans to majority minority census tracts were purchased. Considering only loans directly originated by Charter One causes a dramatic shift in the bank's MSRs, dropping its LMI/MUI MSR from and impressive 1.59 to a poor .59. The decline is equally dramatic when considering minority and non-minority census tracts where the bank's MSR declines from 1.25 to .53 when purchased loans are excluded. Looking at refinance lending shows a lower share of purchased loans, but still extreme disparities.

**Table 1.** Share of Charter One Chicago Area Loans That Were Purchased, 2002

| | Home Purchase | Refinance |
|---|---|---|
| LMI Borrowers | 14.6% | 6.6% |
| MUI Borrowers | 4.9% | 2.0% |
| White Borrowers | 3.4% | 1.6% |
| African American Borrowers | 29.2% | 11.5% |
| Hispanic Borrowers | 43.0% | 16.2% |
| LMI Tracts | 63.0% | 46.5% |
| MUI Tracts | 0.5% | 0.3% |
| Minority Tracts | 60.4% | 42.5% |
| Non-Minority Tracts | 6.2% | 2.8% |

It is troubling that a major lender like Charter One has such a small direct lending presence in LMI and minority communities and appears to have difficulty directly lending to minorities. Charter One's branch presence in LMI and minority areas is not insignificant. According to 2004 FDIC data, 15 percent of Charter One's Chicago area branches are in LMI communities and 19 percent are in minority communities.[3] Both of these numbers generally reflect regional averages.[4] The disparity in Charter One's levels of loan purchases versus direct originations in underserved communities is troubling and indicates that the bank is unwilling or, for some reason, unable to directly do business in LMI and minority areas despite a significant branch presence there.

Although purchased loans are given equal consideration to directly originated loans on CRA exams, we believe directly originated loans provide a much better indicator of the level of a bank's commitment to lending in underserved markets. While purchased loans can add liquidity to mortgage markets, there are questions about the quality of loans in bulk purchase transactions. These bulk purchases often contain well seasoned loans that pass from lender to lender, and it is difficult for banks to screen these loan pools for individual mortgages with abusive features.

We ask that the Federal Reserve take a close look at Charter One's policies of directly originating and purchasing loans in underserved communities. We also ask that Charter One provide details on the nature of the loans purchases and the quality control measures the bank uses to ensure that the loans it

[3] These 2004 data include recently opened offices as well as those added with the 2003 acquisition of Advance Bank which would have improved Charter One's office distribution. Still, in 2002, the bank had a branch network adequate enough to be much more active in LMI and minority communities.
[4] See *Reinvestment Alert #22: Where Banks Aren't.* June 2003. Woodstock Institute: Chicago, IL at www.woodstockinst.org/document/alert22.pdf

purchases do not contain abusive features. In order to allow for this expanded inquiry, we respectfully request that the public comment period for the merger be extended.

We thank you for your consideration.

Sincerely,

Geoff Smith
Project Director

GS/gs