

Community Reinvestment Act Community Development – Examiner Insights

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Agenda

- CRA Evaluation Procedures that Include Community Development (CD)
- Overview of CD
- Geographic Requirements for CD
- Qualifying CD Activities
- Best Practices



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CRA Evaluation Procedures that Include CD

- **Large Institution** – Assets of \$1.216 billion as of 12/31 for two years and at least 12 months of data collected
- **Intermediate Small Institution (ISB)** – Assets over \$304 million and below \$1.216 billion for past two years ([2016 CRA Asset-Size Threshold](#)). Unlike large banks, no time lag since there is no CRA loan data requirement
- **Wholesale/Limited Purpose** – Requires designation from regulator
- **CRA Strategic Plans** – Requires approval from regulator
- **Small Institution** – If the institution chooses, to the extent it enhances credit availability within bank's assessment area

Overview of CD

Five Categories:

- Affordable Housing for Low- or Moderate-Income Individuals (LMI)
- Services to LMI Individuals
- Economic Development by Financing Small Businesses or Small Farms
- Stabilizing and Revitalizing LMI Areas, Designated Disaster Areas, Distressed or Underserved Nonmetropolitan Middle Income Areas
- Support Areas Designated under the Neighborhood Stabilization Programs (NSP)

CD Overview – Affordable Housing

- Affordable Housing [HUD Definition](#) – 30% of income for housing is affordable
 - Calculation:
 1. Area Median Income x 50% = low income
Area Median Income x 80% = moderate income
 2. Divide by 12 = monthly income
 3. Multiply by 30% = affordable housing costs per month
 4. If purchase money, use internet mortgage calculator to determine monthly housing cost
 5. Compare what you calculate to be affordable to rent or purchase price, which are usually included in credit write-ups or investment prospectuses
- For LMI Individuals

CD Overview – Services to LMI

- Community Services targeted to LMI individuals, see [CRA Q&A § .12\(g\)\(2\)-1](#) for examples
- Possible sources:
 - Mission statement of organization
 - Location of organization from FFEIC geocoder
 - Description of service likely to benefit LMI
 - Service is provided to recipients of government assistance

CD Overview – Economic Development

Two part test:

1. Size Test – by Small Business Administration (SBA) standards or have gross annual revenues of \$1 million or less
 - Eligible for SBA's Small Business Investment Company (SBIC) or Small Business Development Company (SBDC) programs
 - SBA [size table](#) by North American Industry Codes (NAICS) system codes
 - Table uses revenue or number of employees
 - Codes are used by lenders on credit approval memos

CD Overview – Economic Development *(continued)*

2. Purpose Test – Permanent job creation, retention or improvement
 - For LMI individuals – [Bureau of Labor Statistics \(BLS\)](#) has wage and employment data by area/occupation (credit documents include Experian or Dunn and Bradstreet reports with borrower employment data),
 - In LMI census tracts (need not be LMI jobs), or
 - Areas designated for redevelopment (need not be LMI jobs or in LMI areas)

*Can presume qualified: SBIC, SBDC, Rural Business Investment Company (BIC), New Markets Venture Capital Company, eligible for New Markets tax credits

CD Overview –

Revitalize and Stabilize

- Attract or retain businesses or residents in certain geographies, see § __.12(g)(4)
 - LMI Census tracts
 - Disaster area
 - Distressed area
 - Underserved area

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CD Overview – Neighborhood Stabilization Programs

- Generally programs approved by HUD and funded by the US Government
- Set up to address areas with high rates of foreclosure

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Geographic Requirements for CD

- Benefits the Assessment Area (AA), see Q&A § __.12(h)-6 and § __.12(h)-7
 - Benefits a broader statewide or regional area that includes the AA
 - Regional Area within a state, such as a tri-county area, the east bay in California, etc.
 - Regional Area that crosses state lines, such as the mid-Atlantic states, Pacific Northwest, etc.
- Does not benefit the AA, can still be considered if
 - Purpose, mandate, or function of the organization or the activity includes serving geographies located in AA, and
 - If institution has been responsive to needs and opportunities within its AA

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Geographic Requirements for CD (continued)

- Nationwide Investments, see Q&A § __.23(a)-2
 - Purpose, mandate, or function of fund serves AA, or broader statewide or regional area that includes the AA
 - Look to fund prospectus for geographic area
 - Investments typically cover multiple years and provide periodic reports on location of projects or businesses funded

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Geographic Requirements for CD – Does it Qualify? – Example #1

- A California bank invests in a nationwide affordable housing fund that targets states on the east coast
- The bank's assessment area is the San Francisco Bay Area
- The nationwide fund will not benefit the San Francisco Bay Area
- The bank has a satisfactory record of meeting the needs within its AA
- **Question: Is the activity a qualified CD investment?**

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Geographic Requirements for CD – Does it Qualify? – Example #1 (continued)

- Answer: No – Affordable housing is one of the categories that qualifies. But, there is no benefit to the bank's assessment area or broader statewide or regional area that includes its assessment area

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Geographic Requirements for CD – Does it Qualify? – Example #2

- A bank in Hawaii makes a donation to the Hawaii food bank that operates on a statewide basis that includes Honolulu, which is in the bank’s assessment area
- The examination just started, so the bank’s performance in the AA is not known
- **Question: Would this donation qualify as a CD donation?**

Geographic Requirements for CD – Does it Qualify? – Example #2 (continued)

- Answer: Yes – Since the food bank operates on a statewide basis that includes the bank’s AA, the donation qualifies without knowing the bank’s performance

Exceptions to Geographic Requirement

- Minority or Women-owned Financial Institutions (MWFIs) and Low-income Credit Unions, see Q&A § __.21(f)-1
 - Geographic requirement does not apply provided the MWFIs or low-income credit union meets the needs of its own AA
 - Examples: Certificates of deposit, loan participations, technical expertise, financial support for CD activities, free or discounted data processing systems or office facilities that benefit these types of institutions

Qualifying CD Activities

- Step 1 – Determine the Purpose
- Step 2 – Two Simple Questions
- Step 3 – Situations to Always Consider
- Step 4 – Documentation
- Step 5 – Qualitative Considerations

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Step 1 – Determine the Purpose

1. Affordable Housing for LMI
2. Community Services Targeted to LMI
3. Economic Development by Financing Small Businesses or Small Farms
4. Revitalization or Stabilization of Designated Areas
5. Support Areas Designated under the Neighborhood Stabilization Program

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Primary Purpose Q&A § __.12(h)-8

- Two approaches:
 1. If the majority of dollars or beneficiaries of the activity are identifiable to one or more of the enumerated CD purposes, then the activity will be considered to possess the requisite primary purpose

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Primary Purpose Q&A §__.12(h)-8 (continued)

- Two approaches (continued):
 2. Alternatively, where the measurable portion of any benefit bestowed or dollars applied to the CD purpose is less than a majority of the entire activity's benefits or dollar value, the activity *may* still be considered to possess the requisite primary purpose and the institution may receive CRA consideration for the entire activity if:
 - **The express, bona fide intent** of the activity, as stated, for example, in a prospectus, loan proposal, or community action plan, is primarily one or more of the enumerated CD purposes;
 - **The activity is specifically structured** (given any relevant market or legal constraints or performance context factors) to achieve the expressed CD purpose; and
 - **The activity reasonably accomplishes, or is reasonably certain to accomplish**, the CD purpose involved

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Step 2 – Two Simple Questions

- Was this activity considered under the retail lending or service tests?
- Does this activity benefit or have the potential to benefit individuals or areas **inside the AA**?

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Some LMI Proxies Q&A §__.12(g)(2)-1

- Service is conducted in an LMI area and targeted to the residents of that area
- Service is offered at workplace to workers who are LMI
- Service provided to students or their families from a school at which the majority of students qualify for free or reduced-price meals
- Service is targeted to individuals who receive Medicaid
- Service is provided to recipients of government assistance programs that have income qualifications equivalent to, or stricter than, the definitions of LMI as defined by CRA Regulations

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Step 3 – Situations to Always Consider Affordable Housing

- Affordable housing for LMI individuals hinges on whether LMI individuals benefit, or are likely to benefit, from the housing, see Q&A § __.12(g)(1)-1
- Institution may receive pro rata consideration for portion of such activities that helps to provide affordable housing to LMI individuals. In other words, the pro rata dollar amount of the total activity will be based on the percentage of units set-aside for affordable housing for LMI individuals, see Q&A § __.12(h)-8

Step 3 – Situations to Always Consider Affordable Housing (continued)

- Example:
 - An institution makes a \$10 million loan to finance a mixed-income housing development in which ten percent of the units will be set aside as affordable housing for LMI individuals. The institution may elect to treat \$1 million of such loan as a CD loan

Step 3 – Situations to Always Consider CD Services

- CD service is a criteria for large banks, intermediate small banks, wholesale and limited purpose banks
- CD service means a service that:
 - Has as its primary purpose CD;
 - Is related to the provision of financial services; and
 - Has not been considered in evaluating the bank's retail banking services under § __.24(d)
- Providing financial services means providing services of the type generally provided by the financial services industry. Providing financial services often involves informing community members about how to get or use credit or otherwise provided credit services or information to the community, see Q&A § __.12(i)-1

Step 3 – Situations to Always Consider CD Services *(continued)*

- Q&As § __.12(i)-2 and § __.12(i)-3 provide more guidance and examples:
 - Services must be provided as a representative of the institution, see Q&A § __.12(i)-2
 - Q&A § __.12(i)-3 includes many examples of community development services

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Step 3 – Situations to Always Consider CD Services *(continued)*

- Q&A § __.12(i)-3 also provides examples of technical assistance activities that are related to providing financial services that might be provided to CD organizations, including:
 - Serving on the board of directors;
 - Serving on a loan review committee;
 - Developing a loan application and underwriting standards;
 - Developing loan-processing systems;
 - Developing secondary market vehicles or programs;
 - Assisting in marketing financial services, including development of advertising and promotions, publications, workshops and conferences;
 - Furnishing financial services training for staff and management;
 - Contributing accounting/bookkeeping services;
 - Assisting in fundraising, including soliciting or arranging investments; and
 - **Providing services reflecting financial institution employees' area of expertise at the institution, such as HR, IT, and legal services**

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Step 3 – Situations to Always Consider CD Services *(continued)*

- Activities that do not take advantage of an employee's financial expertise, such as neighborhood cleanups, do not qualify as providing financial services, see Q&A § __.12(i)-1

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Step 3 – Situations to Always Consider Economic Development

- Size Test and Purpose Test, see Q&A § __.12(g)(3)-1
 - Size Test
 - Activity meets this test if it finances, either directly or through an intermediary, entities that either meet the size eligibility standards of the SBA’s SBDC or SBIC programs, or have gross annual revenues of \$1 million or less
 - Purpose Test
 - Support permanent job creation, retention, and/or improvement for persons who are LMI or in LMI geographies or in areas targeted for redevelopment by Federal, state, local, or tribal governments

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Step 3 – Situations to Always Consider Revitalization or Stabilization

- Activities that revitalize or stabilize a LMI geography are activities that help to attract new, or retain existing businesses or residents, see Q&A § __.12(g)(4)(i)-1
- Some loans may only provide indirect or short-term benefits to LMI individuals in a LMI geography. These loans are not considered to have a CD purpose, see Q&A § __.12(h)-5

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Step 4 – Documentation

- CD Lending, Qualified Investments, and CD Services
 - Date of loan/renewal, investment or service
 - Name and address of the borrower or organization benefiting
 - Dollar amount of the loan or investment
 - Description of the activity and CD purpose
 - Supporting documents (e.g., note, credit approval memo, loan agreement, investment prospectus, side letters, investment partnership agreement, etc.)

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Step 5 – Qualitative Considerations

- Qualitative criteria include the complexity and innovativeness of CD loans, the innovativeness or complexity of qualified investments, and the innovativeness and responsiveness of CD services
- An institution’s performance under qualitative criteria may augment the consideration given to an institution’s performance under the quantitative criteria of the regulations, resulting in a higher level of performance and rating, see Q&A §__.28(b)-1

CRA Best Practices

- Defining Performance Context
- Understanding Assessment Area and Performance Context
- Goal Setting
- Tracking Performance
- Monitoring Performance

Defining Performance Context

- Community Characteristics and Demographics
 - Population
 - Economic conditions
 - Median income levels
 - Distribution of household income
 - Nature of housing stock
 - Housing costs
 - Local industries
- Lending, Investment and Service Opportunities

Defining Performance Context

(continued)

- Bank Characteristics
 - Product offerings and business strategy
 - Institutional capacity and constraints
 - Size and financial condition of the bank
- Past Performance and Performance of Peers
- Written Comments about CRA Performance
- **Other Relevant Information!**

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Understanding AA and Performance Context

- Examiners will consider the responsiveness to credit and CD needs, see Q&A § __.21(a)-2
- Understand the needs in the AA in order to be responsive to those needs
 - To gain an understanding of the credit and CD needs and opportunities in an institution's community, examiners obtain information from community, government, and civic organizations, and sources such as local housing authorities and small business development agencies. Financial institutions can benefit from collaborating with the same organizations

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Understanding AA and Performance Context *(continued)*

- CD activities may differ based on the characteristics of the communities in which the bank operates
- CD activities are not just about geography
- CD activity in the Broader Statewide or Regional Area
- Activities that will not benefit the bank's AAs may enhance performance (Q&A § __.12(h)-6, [July 2014 Outlook Live](#))

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Other Considerations

- Intermediate Small Institution
 - The responsiveness to the opportunities for CD lending, qualified investments, and services
- Large Bank
 - Responsiveness to opportunities
 - Innovativeness and complexity of CD lending, investments, and services
 - The degree to which the qualified investments are not routinely provided by private investors
 - Leadership
- CD Test for Wholesale or Limited-Purpose Banks
 - Use of innovative or complex qualified CD investments, loans, or services
 - The extent to which the investments are not routinely provided by private sector investors; and
 - The bank's total responsiveness to credit and CD needs

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Best Practice – Goal Setting

- Work with Management Team to Determine Appropriate Goals
- Consider Risk Appetite and Resources
- Set Measurable Objectives
 - Number and dollar amount of CD loans and investments
 - Types of CD services
 - Qualified employee service hours
 - Number of seminars or outreach events
 - Consider impact of each activity – number and types of beneficiaries – LMI individuals, small businesses, organizations

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Best Practice – Goal Setting (continued)

- Create an Action Plan
 - Identify key employees
 - Create a plan for reaching LMI individuals
- Resources:
 - [Bureau of Labor Statistics](#)
 - [National Center for Education Statistics](#)

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Best Practice – Training and Tracking

- Train
 - Loan officers, CFO, marketing staff
 - Understand the loan portfolio
 - Develop forms, checklists, and other guides (e.g., credit memos)
- Document
 - Collect and organize data
 - Maintain supporting documentation
 - Develop a centralized process to record (type of activity, how it meets CD purpose, and AA impacted)
- Analyze
 - Periodic review
 - CD Loans – Reporting ([CRA Loan Data Collection Grid](#))

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Best Practice - Tracking

- CD Loans
- CD Investments
 - Equity type
 - Charitable contributions
- CD Services

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Best Practice – Monitoring

- Periodically Review Performance
 - Review spreadsheets
 - Review competitors' CRA public evaluations
 - Maintain contact with government and community groups
- Conduct CRA Self-Assessments

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Resources

- [Interagency CRA Q&A](#) (March 11, 2010) and [Supplemental CRA Q&A](#) (November 20, 2013)
- [Interagency CRA Examination Procedures](#)
- [Notice and Request for Comment on Proposed CRA Q&A](#) (September 8, 2014)
- CRA Public Evaluation Search by Agency: [FRB](#), [FDIC](#), [OCC](#)
- Outlook Lives:
 - [Interagency Q&As Regarding Community Reinvestment](#) (July 17, 2014)
 - [Tips for Reporting Accurate HMDA and CRA Data](#) (November 17, 2010)
- Consumer Compliance Outlook Newsletter Articles:
 - [Transitioning from an ISB to a Large Bank under CRA](#)
 - [CRA: Developing a Strategy for Success](#)
 - [New and Revised Interagency Q&As Regarding CRA: Updates to Community Development Guidance](#)

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Questions?

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