DEMYSTIFYING THE LENDING TEST
The Lending Test evaluates a bank’s record of helping to meet the credit needs of its assessment areas:

- Home mortgage lending
- Small business/farm lending
- Community development lending
- Consumer lending
Management should provide data for all lending they want considered

- Generally, should include all lending data since last exam through a “cut-off” or “as of” date
- This includes data on optional affiliate and consortia/third party lending
- Other loan data
Loan data should be in a format that is conducive to analysis

- HMDA, Small Business/Small Farm, and Consumer Loan data should be in prescribed formats.
- Bank’s responsibility to ensure data is accurate.
- Supplemental records may be needed to receive full consideration for community development loans.
Lending Test Components

- Lending activity
- Assessment area concentration
- Geographic distribution
- Borrower distribution
- Community development lending
- Product innovation and flexible lending practices
Lending Activity

- Foundation of the lending test rating
- Market share and market rank primary way to put activity into context
- Contextual information considered, including credit needs and the competitive environment
- Be prepared to discuss anomalies in the data
Assessment Area Concentration

- Compares lending inside assessment area versus outside
- Performed at the state or bank level
- Does not include affiliate lending
- Business strategy and contextual data may affect this performance criteria
- Be prepared to tell “your story” to explain a low in/out ratio
Geographic Distribution

- Considers performance in lending to all geographies in an assessment area, particularly in low- and moderate-income geographies
- Lending distribution is compared to certain demographic information
- Other comparators might also be used
- Lending gap analysis used to identify conspicuous gaps
- Contextual information may affect conclusion
- Management should be prepared to explain any significant disparities
Example: Geographic Distribution Table – HMDA Loans

<table>
<thead>
<tr>
<th>MSA/Assessment Area:</th>
<th>Total Home Purchase Loans</th>
<th>Low-Income Geographies</th>
<th>Moderate-Income Geographies</th>
<th>Middle-Income Geographies</th>
<th>Upper-Income Geographies</th>
<th>Market Share (%) by Geography *</th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
<td>#</td>
<td>% of Total**</td>
<td>% Owner Occ Units***</td>
<td>% Bank Loans</td>
<td>% Owner Occ Units***</td>
<td>% Bank Loans</td>
</tr>
<tr>
<td>Large City MSA #1</td>
<td>219</td>
<td>44.88</td>
<td>2.63</td>
<td>3.71</td>
<td>15.30</td>
<td>9.18</td>
</tr>
<tr>
<td>Large City MSA #2</td>
<td>269</td>
<td>55.12</td>
<td>1.19</td>
<td>.75</td>
<td>16.35</td>
<td>16.00</td>
</tr>
</tbody>
</table>

* Based on 2006 Peer Mortgage Data

** Home purchase loans originated and purchased in the MA/AA as a percentage of all home loan originated and purchased in the rated area.

***Percentage of Owner Occupied Units is the number of owner occupied units in a particular geography divided by the number of owner occupied housing units in the area based on 2000 Census information.

Focus on performance in low- and moderate-income geographies
Example: Geographic Distribution Table – Small Business Loans

**Geographic Distribution: SMALL LOANS TO BUSINESSES**

<table>
<thead>
<tr>
<th>MSA/Assessment Area:</th>
<th>Total Small Business Loans</th>
<th>Low-Income Geographies</th>
<th>Moderate-Income Geographies</th>
<th>Middle-Income Geographies</th>
<th>Upper-Income Geographies</th>
<th>Market Share (%) by Geography *</th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
<td>#</td>
<td>% of Total**</td>
<td>% of Bus***</td>
<td>% of Bus***</td>
<td>% of Bus***</td>
<td>% of Bus***</td>
</tr>
<tr>
<td>Large City MSA #1</td>
<td>879</td>
<td>76.04</td>
<td>4.45</td>
<td>6.03</td>
<td>32.06</td>
<td>38.57</td>
</tr>
<tr>
<td>Large City MSA #2</td>
<td>277</td>
<td>23.96</td>
<td>0.00</td>
<td>0.00</td>
<td>25.33</td>
<td>23.83</td>
</tr>
</tbody>
</table>

* Based on 2006 Peer Mortgage Data.

** Small loans to businesses originated and purchased in the MA/AA as a percentage of all small loans to businesses originated and purchased in the rated area.


Focus on performance in low- and moderate-income geographies
Lending Gap Analysis
Best Practices

- Perform self assessment
- Generate tables
- Identify areas of poor performance and take action
- Perform the analysis frequently
- Understand your performance context
## Geographic Distribution

### Exercise - 1

Distribution of Home Purchase Loans By Income Level of the Geography

<table>
<thead>
<tr>
<th>Geography Income Level</th>
<th>% of Owner Occupied Housing Units</th>
<th>2006</th>
<th>2007</th>
<th>Total</th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
<td></td>
<td>#</td>
<td>%</td>
<td>#</td>
</tr>
<tr>
<td>Low</td>
<td>3%</td>
<td>5</td>
<td>5%</td>
<td>1</td>
</tr>
<tr>
<td>Moderate</td>
<td>23%</td>
<td>16</td>
<td>17%</td>
<td>26</td>
</tr>
<tr>
<td>Middle</td>
<td>31%</td>
<td>40</td>
<td>44%</td>
<td>30</td>
</tr>
<tr>
<td>Upper</td>
<td>43%</td>
<td>31</td>
<td>34%</td>
<td>22</td>
</tr>
<tr>
<td>Total</td>
<td>100%</td>
<td>92</td>
<td>100%</td>
<td>79</td>
</tr>
</tbody>
</table>
Borrower Distribution

- Considers distribution among borrowers based on income and business size, especially LMI borrowers & small businesses
- Regulators consider different measurements
- Contextual data may affect conclusion
- Management should be prepared to discuss any disparities
**Borrower Profile – Small Business Loans**

Table X – Lending Distribution of Commercial Loans Based on Gross Annual Revenues of the Business

<table>
<thead>
<tr>
<th>Gross Annual Revenue</th>
<th>Less than $50,000</th>
<th>$50,000 to $99,999</th>
<th>$100,000 to $249,999</th>
<th>$250,000 to $499,999</th>
<th>$500,000 to $999,999</th>
<th>$1,000,000 and Greater</th>
</tr>
</thead>
<tbody>
<tr>
<td>Percentage of Businesses by Gross Annual Revenues</td>
<td>11%</td>
<td>25%</td>
<td>31%</td>
<td>13%</td>
<td>8%</td>
<td>12%</td>
</tr>
<tr>
<td>Number of Loans</td>
<td>3</td>
<td>4</td>
<td>2</td>
<td>2</td>
<td>1</td>
<td>6</td>
</tr>
<tr>
<td>Percentage by Number</td>
<td>17%</td>
<td>22%</td>
<td>11%</td>
<td>11%</td>
<td>6%</td>
<td>33%</td>
</tr>
<tr>
<td>Dollar Amount of Loans</td>
<td>$353,025</td>
<td>$308,344</td>
<td>$185,025</td>
<td>$30,050</td>
<td>$50,025</td>
<td>$1,091,154</td>
</tr>
<tr>
<td>Percentage by Dollar Amount</td>
<td>18%</td>
<td>15%</td>
<td>9%</td>
<td>1%</td>
<td>2%</td>
<td>54%</td>
</tr>
</tbody>
</table>
## Borrower Profile – HMDA Loans

### Table X - Distribution of HMDA Loans by Borrower Income

<table>
<thead>
<tr>
<th>Borrower Income Level</th>
<th>% of Aggregate Lending (% of #)</th>
<th>% of Families</th>
<th>2003</th>
<th>2004</th>
<th>Total</th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
<td></td>
<td></td>
<td>#</td>
<td>%</td>
<td>#</td>
</tr>
<tr>
<td>Low</td>
<td>9%</td>
<td>25%</td>
<td>19</td>
<td>21%</td>
<td>18</td>
</tr>
<tr>
<td>Moderate</td>
<td>16%</td>
<td>18%</td>
<td>24</td>
<td>26%</td>
<td>14</td>
</tr>
<tr>
<td>Middle</td>
<td>17%</td>
<td>17%</td>
<td>22</td>
<td>24%</td>
<td>20</td>
</tr>
<tr>
<td>Upper</td>
<td>42%</td>
<td>40%</td>
<td>21</td>
<td>23%</td>
<td>21</td>
</tr>
<tr>
<td>NA</td>
<td>17%</td>
<td>NA</td>
<td>6</td>
<td>6%</td>
<td>6</td>
</tr>
<tr>
<td>Total</td>
<td>100%</td>
<td>100%</td>
<td>92</td>
<td>100%</td>
<td>79</td>
</tr>
</tbody>
</table>
# Borrower Profile
## Exercise 1

### Table X – Distribution of Consumer Loans By Borrower Income Level

<table>
<thead>
<tr>
<th>Borrower Income Level</th>
<th>% of Households</th>
<th>2006</th>
<th>2007</th>
<th>Total</th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
<td></td>
<td>#</td>
<td>%</td>
<td>#</td>
</tr>
<tr>
<td>Low</td>
<td>6%</td>
<td>12</td>
<td>7%</td>
<td>25</td>
</tr>
<tr>
<td>Moderate</td>
<td>25%</td>
<td>42</td>
<td>26%</td>
<td>61</td>
</tr>
<tr>
<td>Middle</td>
<td>36%</td>
<td>72</td>
<td>44%</td>
<td>43</td>
</tr>
<tr>
<td>Upper</td>
<td>33%</td>
<td>39</td>
<td>23%</td>
<td>4</td>
</tr>
<tr>
<td>Total</td>
<td>100%</td>
<td>165</td>
<td>100%</td>
<td>133</td>
</tr>
</tbody>
</table>
## Borrower Profile

**Exercise 2**

<table>
<thead>
<tr>
<th>Gross Annual Revenue (000s)</th>
<th>Area Businesses (D&amp;B)</th>
<th>Bank Loans %</th>
</tr>
</thead>
<tbody>
<tr>
<td>&lt; $100</td>
<td>44%</td>
<td>22%</td>
</tr>
<tr>
<td>$100 to $249</td>
<td>35%</td>
<td>18%</td>
</tr>
<tr>
<td>$250 to $499</td>
<td>12%</td>
<td>20%</td>
</tr>
<tr>
<td>$500 to $999</td>
<td>5%</td>
<td>21%</td>
</tr>
<tr>
<td>≥ $1,000</td>
<td>4%</td>
<td>19%</td>
</tr>
</tbody>
</table>
Responsiveness

- Measures Bank’s responsiveness to low-income areas and borrowers, and to very small businesses
- Reviewed similar to Geographic and Borrower elements
- Multiple measures typically used
- Contextual data may affect conclusions
- Management should be prepared to discuss any disparities
Community Development

- Measures the Bank’s responsiveness and leadership in community development lending
  - Number and amount
  - Complexity and innovativeness

- A community development loan must have a primary purpose of community development
  - An understanding of community development is critical, and this is an evolving area
Community Development

- Affordable housing
- Community services targeted to LMI residents
- Activities that promote economic development by financing small businesses or farms
- Activities that revitalize or stabilize LMI geographies
Community Development

- For non-OTS institutions, revitalizing or stabilizing LMI geographies has been expanded to include:
  - Revitalizing designated disaster areas
  - “Distressed or underserved” middle-income nonmetropolitan areas
Areas designated by the federal government (for example, major disaster declarations by FEMA)

Eligible for 36 months following the date of designation

Refer to FEMA website (http://www.fema.gov) for disaster designations
Distressed or Underserved Area

- Includes middle-income tracts in nonmetropolitan areas
- “Nonmetropolitan” means outside an MSA
- The agencies will publish a list of covered tracts
- Refer to FFIEC website (http://www.ffiec.gov) for listing
### Criteria

<table>
<thead>
<tr>
<th>Distressed</th>
<th>Underserved</th>
</tr>
</thead>
<tbody>
<tr>
<td>- Unemployment rate of at least 1.5 times the national average</td>
<td>- Small population</td>
</tr>
<tr>
<td>- Poverty rate of 20% or more</td>
<td>- Distant from a population center</td>
</tr>
<tr>
<td>- Population loss of 10% or more between the previous and most recent decennial census</td>
<td>- Identified by USDA Urban Influence Codes 7, 10, 11, or 12</td>
</tr>
<tr>
<td>- Net migration loss of 5% or more over the five-year period preceding the most recent census.</td>
<td></td>
</tr>
</tbody>
</table>

* A community is considered distressed if it meets one or more of the above criteria.
Document Your Activities

- Make sure you document the elements that qualify the loan(s) under the regulation
  - Community development primary purpose
  - Area benefited
  - Impact
Be prepared to explain why it’s a community development loan

- Management should be prepared to explain how a loan meets community development purposes
- Time invested in making these loans and tracking the activity helps distinguish an institution’s level of performance
- Contextual data again is reviewed in evaluating performance
Product Innovation

- Looks at the number and complexity of various specialized loan programs the institution offers
  - Be prepared to provide number and $ amount of lending under such programs
Common Issues/Problems

For Bankers

- Data collection
- Community development lending opportunities
- Resource constraints

For Examiners

- Activities not sufficiently documented
- Data integrity
- Data dump w/o analysis
Illegal lending practices

- CRA evaluation adversely affected by discriminatory or other illegal lending practices
- Applies to the bank and its affiliates
- Regulators will consider extent of evidence, bank policies and procedures, and any corrective action taken
- Includes
  - ECOA
  - FHA
  - FTC Act
  - RESPA
  - TILA