



2000

CRA

CONFERENCE

IN APRIL 17, 2000, representatives of the Federal Reserve, the Office of Thrift Supervision, the Office of the Comptroller of the Currency and the Federal Deposit Insurance Corporation gathered as part of the 2000 Community Reinvestment Conference to participate in a question and answer session. Conference attendees were asked to present some of their most perplexing questions regarding CRA, community development and other examination and regulatory concerns. Below are the questions and answers from the session, which have been edited for publication. Thank you to John Gilliam of the OCC, Gregory Imm of the Federal Reserve Bank of San Francisco, George Neeld of the FDIC, and Dave Meders of the OTS for providing the answers, and to Dick Ranftle of the FDIC for moderating the session.

Are grants to organizations that serve minority groups, like the Hispanic Chamber of Commerce or Native American Health Services, qualified investments?

Grants to organizations that serve minority groups are only eligible for CRA consideration if you can show that the group served by the organization is predominantly low- and moderate-income in your community.

If ten banks form a consortium, and the consortium provides seminars for affordable housing developers, can member banks get service test credit?

Financial institutions receive credit for community development services when an employee *of the institution* provides a service related to the provision of financial services to an organization whose primary purpose is community development. In this case, the organization's primary purpose is community development, but if it were the staff *of the consortium* conducting the seminars, the member financial institutions would not be eligible for service test credit. If, on the other hand, a financial institution lent some of its staff to conduct the seminars, that service would be eligible for consideration as a community development service.

Can CRA-qualified investments be reported under "other assets" on bank financial statements? Do the regulators care where they are placed?

The call report dictates how assets are reported. Different types of investment activities may be reported in different places on financial statements. Some investments may be classified as "securities" and others as "other assets". Refer to your CPA or internal accountant to determine how to report different types of investments. Examiners will evaluate qualified investments on their community development attributes, not on where they are located on the financial statement.

What changes in processes or procedures related to CRA could a bank expect to see if its charter is collapsed?

There are two scenarios:

- ▶ The charter being collapsed is wholly owned by the surviving company for the entire time of the review period. The surviving bank would then get consideration for the CRA activities of the collapsed charter for the entire review period.
- ▶ If the charter is acquired during the review period, and the acquiring company decides to collapse it, this is more complicated. The surviving bank gets credit for the collapsed charter's activities from the date of the purchase. Nothing prior to that date is considered.

Examiners would look at the loan-to-deposit ratio created by the surviving charter in the host state. For example, if a charter in California collapsed a charter in Nevada, examiners would look at how much lending the bank was still doing in Nevada, and compare that amount to the deposits in Nevada. This is compared to the annually updated list that provides the standard loan-

to-deposit ratios for each of the 50 states. The loan-to-deposit ratio of the California bank's activity in Nevada must be at least 50% of the Nevada standard.

Do SBA loans over \$ 1 million count as community development loans?

If a loan qualifies as a community development loan, it qualifies. SBA loans are not given special consideration.

Would a community development loan made outside an assessment area 40 miles south count towards a "satisfactory" CRA rating? How about an "outstanding" rating?


Yes, a financial institution would be entitled to count that loan assuming that the performance inside the assessment area is up to par. If the institution has done a poor job in its assessment area, it won't matter what it does outside its assessment area.

Under Arizona law, a spouse must be notified of a credit being entered into by the other spouse in order for the bank to receive payment from any community property assets in the event of default. How can a bank meet the requirements of Regulation B and still protect its position for collectability under the state laws?

A simple notification doesn't violate the provisions of Regulation B. Provisions of Regulation B, at 202.7, subsections (b)2, 3 and 4, give creditors the right to require the signature of a non-signing spouse on any instrument that is necessary, or reasonably believed by the creditor to be necessary, under any applicable state law to make a property being offered as security available to satisfy a debt in the event of default.

Regulation B at 202.5 (c)2, (b)1 provides creditors with the ability to inquire about spousal information and





marital status, if the property being relied upon for repayment is in a community property state. So, if Arizona is a community property state, you have safeguards built into Regulation B that allow this notification without any adverse repercussions under the regulation.

What is the most efficient and preferred way to present exam information to examiners?

It's easiest, especially with small business and small farm micro-loan data, to submit it on disc or CD-ROM, which allows examiners to slice and dice the numbers to the extent necessary. Examiners have seen community development information presented in a wide variety of tables, charts and lists that convey the necessary information. Ideally, the important pieces are presented in a list that contains at least the following:

- Identifies the borrower;
- Tells which component of the community development definition the transaction falls under, for example: affordable housing or economic revitalization;
- Explains how the transaction meets the community's need including the percentage of low- or moderate-income served;
- Identifies the transaction as a loan or investment and includes the dollar amount.

Examiners can easily review this list, and if it's clear that the transaction qualifies, there might not be a need to report additional details.

For HMDA reporting, a borrower's income on a purchased loan is an optional item. If a bank decided not to report this item under HMDA, would the bank still receive credit if the borrower was low- or moderate-income,

provided this information is available in the borrower's file?

You could still receive credit as long as you provide the necessary documentation for the examiners during the review.

Explain the logic of not including letters of credit in the "community development" loan category.

Letters of credit do in fact "count" under the community development loan category. The regulations state that the examiner, in addition to considering originations and purchases, "will also consider any other loan data the bank may choose to provide, including data on loans outstanding, commitments and letters of credit."

If interest is credited back to a certificate of deposit, must the bank provide a notice of this activity to the account holder per Regulation DD?

Generally, adding back or crediting earned interest isn't a triggering action requiring predisclosure per Regulation DD. The only case where you would have to disclose this is if you were providing periodic statements for time deposits. If there is one, the bank must show the earned interest on the periodic statement [Sec. 230.6(a)(2)].

What concessions, if any, are given under the service and investment tests for a financial institution that is making the transition from a small to a large institution? What is the ultimate impact on the CRA rating?

Concessions can be made depending on the totality of the circumstances. The contextual data that go into the evaluation for the large institution test take into account things factors such as business strategy, unusual growth, competition in the marketplace, and any other unusual elements within the marketplace that might impact performance. For an institution in transition from small to large,

any of these factors can be used to explain any unusual numbers or what would appear to be a negative trend.

We have been offered below market rates for deposits in community development credit unions. Can examiners give any "recognition" for the "lost" interest on the investments?

No. However, one can always give contextual information on investments, including any information on "lost" interest. The examiner can consider this information, but it will not necessarily end up in any final report.

Do loans to businesses located in federal or state enterprise zones automatically qualify as community development loans?

No. Even if the business is located in an enterprise zone, the loan doesn't automatically qualify. The loan must meet the community development definition, for instance by providing affordable housing, revitalizing the area or creating permanent jobs. Also, loan funds must help the business participate in the incentive programs of that enterprise zone, such as tax credits or training credits.

To what extent does a bank's community development loan performance add to or detract from its geographic distribution performance? The lending test seems to be based solely on low- and moderate-income distribution.

Lending performance is primarily based on low- and moderate-income loan distribution. Community development loans add value to a large bank's performance and can help fill in weak spots. Low- and moderate-income and community development loans are analyzed separately unless they support each other.

Small business loans are loans of \$1 million or less or to businesses that meet SBDC/SBIC size standards. These are vastly different as the SBDC standard is \$6 million in net worth with income after taxes of \$2 million. How does the SBIC/SBDC standard apply? (Follow-up question answered by Fred Mendez)

You are correct in saying that these two standards are vastly different. That is because they apply to two different activities, small business lending and community development lending. Any loan to a business in an amount less than \$1 million and reported in Schedule RC-C, part I, item 1.e and Schedule RC-C, part I, item 4.a of the Consolidated Report of Condition and Income ("Call Report") is considered a small business loan and should be reported as such. Everything else is eligible to be a community development loan, including loans in an amount less than \$1 million that are not reported on lines 1.e or 4.a as mentioned above.

According to the Call Report, a small business loan is defined as:

- ▶ Loans to a for-profit entity not secured by real estate and equal to or less than \$1 million;
- ▶ Permanent loans to a for-profit entity secured by nonresidential real estate and equal or less than \$1 million;
- ▶ Permanent loans to a nonprofit entity secured by non-farm, non-residential real estate or production payments and, equal to or less than \$1 million with or without primary purpose consistent with the definition of community development.

The second key definition is that of community development. The regulation defines community development to mean:

- ▶ Affordable housing (including multi-family rental housing) for low- or moderate-income individuals;
- ▶ Community services targeted to low- or moderate-income individuals;
- ▶ Activities that promote economic development by financing businesses or farms that meet the size eligibility standards of 13CFR121.301 (SBDC/SBIC parameters) or have gross annual revenues of \$1 million or less; or
- ▶ Activities that revitalize or stabilize low- or moderate-income geographies.

Keep in mind that the third bullet point in the definition of community development does not mention small businesses, only those activities which promote economic development.

Our institution has made a public commitment, part of which is a consumer loan component. In the past we have not provided consumer loan information to examiners since it is optional. Will this commitment open up our consumer lending for review by regulators during CRA exams?

No. Commitments are not legally binding, but there is a risk to the bank's reputation if the bank is unable to fulfill the commitment. The bank's performance under the commitment doesn't affect the examination, but the bank might want to show the results to the examiners to demonstrate the bank's responsiveness to a variety of community credit needs. The commitment by itself doesn't trigger an examiner's interest. However, the pending Sunshine regulations may change how commitments are evaluated. **CI**

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