



# The BIG Bank World of CRA

On November 12, 1999, President Clinton signed the Gramm-Leach-Bliley Act of 1999 into law, effectively repealing restrictions on bank affiliation with securities firms and insurance companies contained in the depression era Glass-Steagall Act. The Gramm-Leach-Bliley Act now permits banks, insurance companies, securities firms and other financial institutions to affiliate under common ownership and offer their customers a complete range of financial services. This Act places certain conditions on these new activities, one of which is that all of a holding company's insured depository institution subsidiaries have at least a satisfactory Community Reinvestment Act (CRA) rating.

The implementation of the Gramm-Leach-Bliley Act comes at a time when large complex banking organizations (LCBOs) are under pressure from shareholders to provide their products and services in a streamlined and cost-efficient manner in order to maintain strong earnings growth while at the same time satisfying community and

customer needs. To better understand how LCBO CRA activity is evolving in this environment, interviews were conducted with senior representatives from twelve LCBOs about how they manage their CRA activities from the holding company level down to their non-bank subsidiaries. This broad question encompasses many other questions such as how effective they have been at developing institution-wide CRA strategies and how they have balanced the needs of their communities with the need to streamline the delivery of their products and services.

This article will summarize the information gathered from those interviews with the goal of providing our readers with a snapshot of how complex institutions structure and manage their CRA activities to serve low- and moderate-income individuals and communities. The answers contained in this article may cause financial institution representatives to think differently about their CRA programs or at least see them in a larger context. For community-based organization representatives this information will offer insight into the opportunities, limitations and

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conditions associated with bank partnerships.

The twelve LCBOs that provided information about how their CRA activities are managed include:

- Citigroup
- Chase
- First Union
- HSBC Bank USA
- Key Corporation
- National City Bank
- Sun Trust Bank
- Union Bank of California
- US Bank
- Wachovia
- Washington Mutual
- Wells Fargo

The information they provided focuses on four areas:

- **The LCBO:** the geographies they serve, their subsidiaries, and their primary lines of business
- **Subsidiaries:** those subsidiaries that contribute to the CRA-related goals and activities of the LCBO
- **CRA program:** overall CRA strategy; the decision makers in the areas of CRA-related lending, investment and service activities of the institution and any subsidiary; and how success is measured
- **Organization structure:** where the various CRA-related activities are housed or organized within the LCBO

### THE LCBOs

The twelve LCBOs that participated in this study varied in scope and size from \$33 billion in assets serving three states to \$716 billion in assets and serving most of the country. All of these LCBOs concentrate their business activity in major metropolitan areas because these areas represent their biggest marketplaces and thus the largest concentration of opportunities.

Eleven of the twelve had centralized management systems where strategies

and decisions are developed at the holding company level. Eleven of the twelve considered their organization to be full service financial corporations striving to provide their customers with as wide an array of financial products as possible. After discussing the context under which their CRA activities are conducted, the representatives interviewed claimed that they could not be “all things to all people.” The bottom line is that these LCBOs have a core line of business they rely on during volatile times—be it small business, consumer or home financing products—and are quick to re-evaluate product lines that are not competitive or are less profitable. The one LCBO that had a decentralized structure allows each bank within the various states they are chartered to serve significant autonomy to run the way the local president deems best.

### SUBSIDIARIES

Four of the LCBOs interviewed have subsidiaries that serve the entire nation with either mortgage or credit card products. One is actively engaged in check cashing to tap into the large population of unbanked individuals. Three of the LCBOs offer sub-prime lending products through finance company subsidiaries. Ten of the twelve LCBOs interviewed stated that their subsidiaries play virtually a non-existent role in the LCBO's overall CRA strategy even though many of these serve low- and moderate-income individuals and communities. The primary reason given for why these subsidiaries do not play a more prominent role in the LCBO's CRA program had to do primarily with the difficulty in managing and collecting the right data to report to their relevant supervisory agency. As such, almost all the CRA-related activities of these LCBOs that are evaluated under the CRA examination process continue to be performed at the insured depository institution level.

### LCBO STRUCTURE & CRA PROGRAMS

All of the LCBOs interviewed said that the majority of their CRA-eligible business comes from metropolitan areas. This concentration of activity is due primarily to the concentration of population and, therefore, greater economies of scale in the development of products and services targeted to low- and moderate-income areas and individuals. The ability to develop products of sufficient scale and volume helps to ensure some measure of success and profitability. Other less obvious motivations exist in metropolitan area markets to encourage LCBO innovation in providing financial products to low- and moderate-income geographies. These motivations include:

- Partnerships opportunities with sophisticated community-based organizations that can provide guidance and support to LCBOs looking for ways to satisfy their obligations under the CRA
- Consumer advocacy organizations, the media and other advocates for low- and moderate-income individuals which can focus public scrutiny on the activities of these LCBOs and their impact on low- and moderate-income geographies

Given the benefits of concentrating CRA activities in major markets, rural areas are more of a challenge for LCBOs, making partnerships even more critical to leverage limited LCBO resources in these areas. All of the LCBO representatives interviewed defined the role of intermediaries for CRA-related lending, service and investment activities (CRA partners) as filling financial service gaps created for reasons that range from geography and human resources to lack of expertise.

When asked what qualities they look for in CRA partners, the LCBO representatives were unanimous in describing their “ideal” as:

- Having experienced management and talented staff
- Demonstrating a strong track record
- Having a clear and realistic business plan
- Serving a large geographic area or population base

### **CRA STRUCTURE AND DECISION MAKING**

Irrespective of whether the LCBO interviewed had a centralized or decentralized management structure, the strategy for how CRA activities are conducted is similar. For LCBOs with a centralized structure, the most senior level executives overseeing the institution's CRA activity develop a strategy with the directors of the LCBO's business lines. Previous years' CRA-eligible activity by product line is used as a benchmark from which to develop this strategy, as is consideration of competitive and demographic information gathered by internal staff and through the CRA Public Evaluation of competing financial institutions. To ensure its alignment with the business strategy of the corporation as a whole, the new strategy is first communicated to the LCBO's executive committee. From there, the strategy is conveyed to the regional directors for each business line as well as to regional representatives who serve as "CRA experts." CRA experts specialize in CRA-related lending and investment projects by business line that, due to their complexity or unique nature, may not be easily managed by local branch or lending staff.

For the LCBO with a decentralized structure, a similar process takes place but at the regional level with the CRA and business line directors communicating their strategy to the president and executive committee of the local bank. The strategy of each local bank is then conveyed to the executive committee at the holding company level to

ensure consistency with the business strategy of the corporation as a whole.

The LCBO representatives interviewed all consider the major portion of their CRA-eligible activities (mostly in lending) to be conventional products that can be provided by any of the institutions' representatives. Community development service activities are also typically handled through conventional banking channels with local staff having broad authority. Twenty-five years of complying with the CRA has resulted in the standardization of many of the small business, consumer, home mortgage and charitable products that represent the bulk of CRA-eligible activities reviewed under the existing regulation. Those financial products and services that cannot be easily "standardized" are handled either through CRA partners (essentially outsourcing these activities) or through specialized teams of CRA experts who act as advisors to local lending or branch staff. In one fashion or another, all of the LCBOs interviewed use CRA experts to provide technical assistance to local institution staff or directly coordinate more complicated deals that are not "off-the-shelf."

Managing CRA-eligible qualified investments are a bit more complicated than CRA-related lending and service activities. Local representatives have fairly broad authority to grant funds to local organizations. Larger scale investments in organizations that do housing or small business lending will typically require the involvement of the regional CRA expert and sometimes may require approval from the senior executive overseeing CRA for the LCBO. In the case of the decentralized LCBO, approval from the executive overseeing CRA for the local institution may be necessary.

In all but the most complicated of cases, LCBOs typically have three layers of decision makers:

1. Branch and local staff
2. Regional CRA expert
3. Senior or executive vice president in charge of CRA

In the case of specialized and/or complicated initiatives, the decision-making structure can become complex. For example, a multi-bank initiative to create a community loan fund would require at a minimum the involvement of:

- a representative knowledgeable about community needs
- a representative to provide guidance concerning the CRA implications of the initiative (usually the regional CRA expert)
- a senior level CRA executive to authorize participation in the initiative
- a senior level treasury executive to approve the resources necessary for the institution to invest in the initiative

As LCBOs experiment in trying to find the ideal corporate structure, complex decision-making processes may be further complicated by reorganizations, which have become somewhat commonplace. Even when a local representative reports to in terms of CRA activity and business products may change from one period to the next. The senior level executives we spoke to at these LCBOs were quite honest in admitting that sometimes their staff isn't aware of who is next in line in the decision-making process.

The effects that these reorganizations and complex structures have on local markets ties in with the desire of these LCBOs to coordinate low maintenance partnerships. Local staff of LCBOs typically have responsibility over a large geographic area or population base



## ABOUT THE AUTHOR

FRED MENDEZ is a senior community investment specialist for the Federal Reserve Bank of San Francisco. Since joining the Federal Reserve in April of 1993, Fred has acted as a liaison between financial institutions and their community to promote public/private partnerships for economic development. In this capacity he has advised community development lending organizations on regulatory matters surrounding consortia and community development lending; encouraged the evolution of the secondary market into the community development arena; researched legal and commercial issues to facilitate the flow of capital to Native American lands; and educated both the lending and non-profit community about community reinvestment requirements, community development lending, the secondary market, fair lending legislation and bank reform issues. Fred has published articles on the Community Reinvestment Act, community development lending, and Native American economic development, and has made numerous presentations at both national and regional banking conferences.

Prior to joining the Federal Reserve, Fred worked on the floors of both the Pacific Coast and New York Stock Exchanges, was a secondary market trade coordinator for Continental Savings of America and a financial industry specialist for Dow Jones/Telerate. He holds two degrees in economics with an emphasis in economic development and monetary policy.

and are limited in their abilities to serve on nonprofit boards or committees. Regional CRA experts serve even larger geographies and are therefore under even greater time and resource constraints. The most senior level executives overseeing an institution's CRA activity usually aren't even in the same state as many of the institution's partner organizations. This often means they must prioritize their involvement towards large and highly visible national organizations. Also as a result, the seniority level of bank representatives on nonprofit boards and committees has declined and the amount of time an institution's representative can dedicate to a particular organization is limited.

The ideal partner in this changing environment may be one that does not require the most senior level representative to actively participate on a board or committee. A few LCBO representatives went so far as to question their institution's requirement for a board or committee seat in return for financial support as long as the existing board or committee participants include senior representatives from small- or mid-sized financial institutions that can appropriately manage the use of funds.

## CONCLUSION

While the information gathered through our interviews may not be new or groundbreaking, it underscores the systematic approach required to develop a successful CRA-strategy within large complex banking organizations. The aggregate of the responses reveals four areas of priority

common among all of the LCBOs as follows:

1. Concentrating resources on areas that have the greatest need and the greatest opportunity for success and profitability (i.e. major metropolitan areas)
2. Institutionalizing CRA products and services to reduce the need for costly, specialized programs and targeted products
3. Outsourcing financial products and services that cannot be provided efficiently or profitably by the LCBO to organizations that have experienced management, have a demonstrated track record, have a realistic business plan, serve a large geographic area or population base and do not ask for a lot in return
4. Creating a lean structure for dealing with specialized and complicated CRA projects

Looking ahead, LCBOs will continue to look for ways to serve the credit needs of low- and moderate-income individual and geographies, but will do so as organizations under pressure to provide these products and services in a streamlined and cost-efficient manner. Community development intermediaries that specialize in serving low- and moderate-income individuals and geographies will have the opportunity to play a larger role as LCBOs look for ways to outsource some of their CRA activities. *CI*