

**QUALIFIED INVESTMENT** means a lawful investment, deposit, membership share or grant that has as its primary purpose community development

**COMMUNITY DEVELOPMENT** means:

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

## QUESTIONS AND ANSWERS FOR QUALIFIED INVESTMENTS

§§ \_\_.12(i) & 563e.12(h) – 5:

*Must there be some immediate or direct benefit to the institution's assessment area(s) to satisfy the regulation's requirement that qualified investments and community development loans or services benefit an institution's assessment area(s) or a broader statewide or regional area that includes the institution's assessment area(s)?*

**A5.** No. The regulation recognizes that community development organizations and programs are efficient and effective ways for institutions to promote community development. These organizations and programs often operate on a statewide or even multi-state basis. Therefore, an institution's activity is considered a community development loan or service or a qualified investment if it supports an organization or activity that covers an area that is larger than, but includes, the institution's assessment area(s). The institution's assessment area(s) need not receive an immediate or direct benefit from the institution's specific participation in the broader organization or activity, provided that the purpose, mandate, or function of the organization or activity includes serving geographies or individuals located within the institution's assessment area(s).

In addition, a retail institution that, considering its performance context,

has adequately addressed the community development needs of its assessment area(s) will receive consideration for certain other community development activities. These community development activities must benefit geographies or individuals located somewhere within a broader statewide or regional area that includes the institution's assessment area(s). Examiners will consider these activities even if they will not benefit the institution's assessment area(s).

§§ \_\_.12(i) & 563e.12(h) – 6:

*What is meant by the term "regional area"?*

**A6.** A "regional area" may be as small as a city or county or as large as a multi state area. For example, the "mid-Atlantic states" may comprise a regional area. Community development loans and services and qualified investments to statewide or regional organizations that have a bona fide purpose, mandate or function that includes serving the geographies or individuals within the institution's assessment area(s) will be considered as addressing assessment area needs. When examiners evaluate community development loans and services and qualified investments that benefit a regional area that includes the institution's assessment area(s), they will

consider the institution's performance context as well as the size of the regional area and the actual or potential benefit to the institution's assessment area(s). With larger regional areas, benefit to the institution's assessment area(s) may be diffused and, thus less responsive to assessment area needs.

In addition, as long as an institution has adequately addressed the community development needs of its assessment area(s), it will also receive consideration for community development activities that benefit geographies or individuals located somewhere within the broader statewide or regional area that includes the institution's assessment area(s), even if those activities do not benefit its assessment area(s).

§§ \_\_.12(i) & 563e.12(h) – 7:

*What is meant by the term "primary purpose" as that term is used to define what constitutes a community development loan, a qualified investment or a community development service?*

**A7.** A loan, investment or service has as its primary purpose community development when it is designed for the express purpose of revitalizing or stabilizing low- or moderate-income areas, providing affordable housing for, or community services targeted to, low- or moderate-income persons, or promoting economic development by fi

nancing small businesses and farms that meet the requirements set forth in §§ \_\_.12(h) or 563e.12(g). To determine whether an activity is designed for an express community development purpose, the agencies apply one of two approaches. First, if a majority of the dollars or beneficiaries of the activity are identifiable to one or more of the enumerated community development purposes, then the activity will be considered to possess the requisite primary purpose. Alternatively, where the measurable portion of any benefit bestowed or dollars applied to the community development purpose is less than a majority of the entire activity's benefits or dollar value, then the activity may still be considered to possess the requisite primary purpose if (1) 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 community development purposes; (2) the activity is specifically structured (given any relevant market or legal constraints or performance context factors) to achieve the expressed community development purpose; and (3) the activity accomplishes, or is reasonably certain to accomplish, the community development purpose involved. The fact that an activity provides indirect or short-term benefits to low- or moderate-income persons does not make the activity community development, nor does the mere presence of such indirect or short-term benefits constitute a primary purpose of community development. Financial institutions that want examiners to consider certain activities under either approach should be prepared to demonstrate the activities' qualifications.

§§ \_\_.12(s) & 563e.12(r) – 2:

*Are mortgage-backed securities or municipal bonds "qualified investments"?*

**A2.** As a general rule, mortgage-backed securities and municipal bonds are not

qualified investments because they do not have as their primary purpose community development, as defined in the CRA regulations. Nonetheless, mortgage-backed securities or municipal bonds designed primarily to finance community development generally are qualified investments.

Municipal bonds or other securities with a primary purpose of community development need not be housing-related. For example, a bond to fund a community facility or park or to provide sewage services as part of a plan to redevelop a low-income neighborhood is a qualified investment. Housing-related bonds or securities must primarily address affordable housing (including multifamily rental housing) needs in order to qualify. See also § \_\_.23(b) – 2.

§§ \_\_.12(s) & 563e.12(r) – 3:

*Are Federal Home Loan Bank stocks and membership reserves with the Federal Reserve Banks "qualified investments"?*

**A3.** No. Federal Home Loan Bank (FHLB) stock and membership reserves with the Federal Reserve Banks do not have a sufficient connection to community development to be qualified investments. However, FHLB member institutions may receive CRA consideration for technical assistance they provide on behalf of applicants and recipients of funding from the FHLB's Affordable Housing Program. See §§ \_\_.12(j) & 563e.12(i) – 3.

§§ \_\_.12(s) & 563e.12(r) – 4:

*What are examples of qualified investments?*

**A4.** Examples of qualified investments include, but are not limited to, investments, grants, deposits or shares in or to:

- Financial intermediaries (including, Community Development Financial Institutions (CDFIs), Community Development Corporations (CDCs),

minority- and women-owned financial institutions, community loan funds, and low-income or community development credit unions) that primarily lend or facilitate lending in low- and moderate-income areas or to low- and moderate-income individuals in order to promote community development, such as a CDFI that promotes economic development on an Indian reservation

- Organizations engaged in affordable housing rehabilitation and construction, including multifamily rental housing

- Organizations, including, for example, Small Business Investment Companies (SBICs) and specialized SBICs, that promote economic development by financing small businesses

- Facilities that promote community development in low- and moderate-income areas for low- and moderate-income individuals, such as youth programs, homeless centers, soup kitchens, health care facilities, battered women's centers, and alcohol and drug recovery centers

- Projects eligible for low-income housing tax credits

- State and municipal obligations, such as revenue bonds, that specifically support affordable housing or other community development

- Not-for-profit organizations serving low- and moderate-income housing or other community development needs, such as counseling for credit, homeownership, home maintenance, and other financial services education

- Organizations supporting activities essential to the capacity of low- and moderate-income individuals or geographies to utilize credit or to sustain economic development, such as, for example, day care operations and job training programs that enable people to work

§§ \_\_.12(s) & 563e.12(r) – 5:

*Will an institution receive consideration for charitable contributions as "qualified investments"?*

**A5.** Yes, provided they have as their primary purpose community development as defined in the regulations. A charitable contribution, whether in cash or an in-kind contribution of property, is included in the term “grant.” A qualified investment is not disqualified because an institution receives favorable treatment for it (for example, as a tax deduction or credit) under the Internal Revenue Code.

§§ \_\_.12(s) & 563e.12(r) – 6:

*An institution makes or participates in a community development loan. The institution provided the loan at below-market interest rates or “bought down” the interest rate to the borrower. Is the lost income resulting from the lower interest rate or buy-down a qualified investment?*

**A6.** No. The agencies will however, consider the innovativeness and complexity of the community development loan within the bounds of safe and sound banking practices.

§§ \_\_.12(s) & 563e.12(r) – 7:

*Will the agencies consider as a qualified investment the wages or other compensation of an employee or director who provides assistance to a community development organization on behalf of the institution?*

**A7.** No. However, the agencies will consider donated labor of employees or directors of a financial institution in the service test if the activity is a community development service.

§ \_\_.23(b) Exclusion

§ \_\_.23(b) – 1:

*Even though the regulations state that an activity that is considered under the lending or service tests cannot also be considered under the investment test, may parts of an activity be considered under one test and other parts be considered under another test?*

**A1.** Yes, in some instances the nature of an activity may make it eligible for consideration under more than one of the performance tests. For example, certain investments and related support provided by a large retail institution to a CDC may be evaluated under the lending, investment, and service tests. Under the service test, the institution may receive consideration for any community development services that it provides to the CDC, such as service by an executive of the institution on the CDC’s board of directors. If the institution makes an investment in the CDC that the CDC uses to make community development loans, the institution may receive consideration under the lending test for its pro-rata share of community development loans made by the CDC. Alternatively, the institution’s investment may be considered under the investment test, assuming it is a qualified investment. In addition, an institution may elect to have a part of its investment considered under the lending test and the remaining part considered under the investment test. If the investing institution opts to have a portion of its investment evaluated under the lending test by claiming a share of the CDC’s community development loans, the amount of investment considered under the investment test will be offset by that portion. Thus, the institution would only receive consideration under the investment test for the amount of its investment multiplied by the percentage of the CDC’s assets that meet the definition of a qualified investment.

§ \_\_.23(b) – 2:

*If home mortgage loans to low- and moderate-income borrowers have been considered under an institution’s lending test, may the institution that originated or purchased them also receive consideration under the investment test if it subsequently purchases mortgage-backed securities that are*

*primarily or exclusively backed by such loans?*

**A2.** No. Because the institution received lending test consideration for the loans that underlie the securities, the institution may not also receive consideration under the investment test for its purchase of the securities. Of course, an institution may receive investment test consideration for purchases of mortgage-backed securities that are backed by loans to low- and moderate-income individuals as long as the securities are not backed primarily or exclusively by loans that the same institution originated or purchased.

§ \_\_.23(e) Performance criteria

§ \_\_.23(e) – 1:

*When applying the performance criteria of § \_\_.23(e), may an examiner distinguish among qualified investments based on how much of the investment actually supports the underlying community development purpose?*

**A1.** Yes. Although § \_\_.23(e)(1) speaks in terms of the dollar amount of qualified investments, the criterion permits an examiner to weight certain investments differently or to make other appropriate distinctions when evaluating an institution’s record of making qualified investments. For instance, an examiner should take into account that a targeted mortgage-backed security that qualifies as an affordable housing issue that has only 60 percent of its face value supported by loans to low- or moderate-income borrowers would not provide as much affordable housing for low- and moderate-income individuals as a targeted mortgage-backed security with 100 percent of its face value supported by affordable housing loans to low- and moderate-income borrowers. The examiner should describe any differential weighting (or other adjustment), and its basis in the Public Evaluation. However, no matter how a qualified investment is handled for purposes

of § \_\_.23(e)(1), it will also be evaluated with respect to the qualitative performance criteria set forth in § \_\_.23(e)(2), (3) and (4). By applying all criteria, a qualified investment of a lower dollar amount may be weighed more heavily under the Investment Test than a qualified investment with a higher dollar amount, but with fewer qualitative enhancements.

§ \_\_.23(e) – 2:

*How do examiners evaluate an institution's qualified investment in a fund, the primary purpose of which is community development, as that is defined in the CRA regulations?*

**A2.** When evaluating qualified investments that benefit an institution's assessment area(s) or a broader statewide or regional area that includes its assessment area(s), examiners will look at the following four performance criteria:

1. The dollar amount of qualified investments;
2. The innovativeness or complexity of qualified investments;
3. The responsiveness of qualified investments to credit and community development needs; and
4. The degree to which the qualified investments are not routinely provided by private investors.

With respect to the first criterion, examiners will determine the dollar amount of qualified investments by relying on the figures recorded by the institution according to generally accepted accounting principles (GAAP). Although institutions may exercise a range of investment strategies, including short-term investments, long-term investments, investments that are immediately funded, and investments with a binding, up-front commitment that are funded over a period of time, institutions making the same dollar amount of investments over the same number of years, all other performance criteria being equal, would receive the

same level of consideration. Examiners will include both new and outstanding investments in this determination. The dollar amount of qualified investments also will include the dollar amount of legally binding commitments recorded by the institution according to GAAP.

The extent to which qualified investments receive consideration, however, depends on how examiners evaluate the investments under the remaining three performance criteria—innovativeness and complexity, responsiveness, and degree to which the investment is not routinely provided by private investors. Examiners also will consider factors relevant to the institution's CRA performance context, such as the effect of outstanding long-term qualified investments, the pay-in schedule, and the amount of any cash call, on the capacity of the institution to make new investments.

§ \_\_.25(d) Indirect activities

§ \_\_.25(d) – 1:

*How are investments in third party community development organizations considered under the community development test?*

**A1.** Similar to the lending test for retail institutions, investments in third party community development organizations may be considered as qualified investments or as community development loans or both (provided there is no double counting), at the institution's option, as described above in the discussion regarding §§ \_\_.22(d) and \_\_.23(b).

§ \_\_.26(a) Performance criteria

§ \_\_.26(a) – 1:

*May examiners consider, under one or more of the performance criteria of the small institution performance standards, lending-related activities, such as community development loans and lending-related qualified investments, when evaluating a small institution?*

**A1.** Yes. Examiners can consider "lending-related activities," including community development loans and lending-related qualified investments, when evaluating the first four performance criteria of the small institution performance test. Although lending-related activities are specifically mentioned in the regulation in connection with only the first three criteria (i.e., loan-to-deposit ratio, percentage of loans in the institution's assessment area, and lending to borrowers of different incomes and businesses of different sizes), examiners can also consider these activities when they evaluate the fourth criteria—geographic distribution of the institution's loans.

§ \_\_.26(a) – 5:

*Under the small institution performance standards, how will qualified investments be considered for purposes of determining whether a small institution receives a satisfactory CRA rating?*

**A5.** The small institution performance standards focus on lending and other lending-related activities. Therefore, examiners will consider only lending-related qualified investments for the purposes of determining whether the small institution receives a satisfactory CRA rating.

§ \_\_.26(b) – 2:

*Will a small institution's qualified investments, community development loans, and community development services be considered if they do not directly benefit its assessment area(s)?*

**A2.** Yes. These activities are eligible for consideration if they benefit a broader statewide or regional area that includes a small institution's assessment area(s), as discussed more fully in §§ \_\_.12(i) & 563e.12(h) – 6. **CI**