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The CRA Strategic Plan Option: Should We Bother?

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We have all heard examiners and consultants espouse the virtues of the Strategic Plan, but why should we consider the Strategic Plan Option (SPO) as a method for measuring compliance with the Community Reinvestment Act? What factors need to be considered in choosing the best method of measuring compliance with the CRA? I have asked myself and others these questions many times, and the answers vary widely. Banker's reactions to the SPO, and whether to consider it, have become almost comical. They include "You must be crazy," "It's too expensive to develop a Plan," and "Publicly stating our lending goals for our competitors to see? Allowing public comment on our goals? No way!"

Examiners and consultants, on the other hand, are consistent in their support of the SPO. Some examiners "sell" the SPO like used car salesmen. Whether it is the right car for us is not their concern. Others take a more helpful approach, presenting the benefits of the SPO and acknowledging that it is not the right choice for every bank. Since the release of the new CRA examination guidelines, examiners have presented the SPO as an opportunity for banks to: (1) design their own CRA test; (2) remove examination uncertainty; and (3) remove or reduce examiner subjectivity.

Many consultants understand the huge undertaking necessary to develop a CRA Strategic Plan and will help an institution evaluate whether the Plan is a viable option and whether it is appropriate for that institution. Others are less thoughtful in their analysis, and simply recommend the SPO without a solid review of whether the SPO is the best choice for the bank.

So whats a bank to do? Who do we listen to? I say listen to everyone. They are all correct. The SPO is a choice worthy of consideration. This view is based on a number of factors, including the information presented by examiners, consultants and bankers, and our situation at Silicon Valley Bank (SVB).

I strongly disagree with anyone who believes that satisfactory performance under the old examination guidelines means satisfactory performance under the new guidelines. This opinion equates effort with results. While there is usually a relationship between effort and results, it is not absolute. The old guidelines required that, among other things, we ascertain the credit needs of our delineated community. The new regulation is performance-based, measuring how well we meet those needs, a totally different measurement of performance. However, it seems likely that if your bank did not perform well under the old guidelines it will not perform well under the Large Retail Bank test.... unless you are extremely lucky.

I have also heard people say that banks no longer need to ascertain credit needs. This is absolutely not the case. These people may have a naive view of what it takes to run a successful business. We must continue to ascertain needs. How can any bank be responsive to credit needs without knowing what they are? It is true, however, that we no longer need to document our ascertainment efforts.

Finally, I must also disagree with those who believe that the CRA compliance burden has been significantly reduced with the changes in the examination

procedures. While it is true that we no longer need to document our every "CRA activity" and contact, we do need to increase our record keeping and loan tracking. This record keeping is necessary to meet the new data reporting requirements of the regulation and to periodically measure performance. Because the new guidelines require data collection and reporting, they appear to reduce examiner discretion; they also provide banks with an increased opportunity for self assessment. However, until we have gone a few rounds under the new guidelines and resolved most of the open questions (such as what constitutes a "substantial majority"), self evaluation will not be an exact science. Additionally, banks may want to record and analyze data regarding loans that are not reportable in order to uncover all loans that meet the stated goals of the CRA.

These reactions and opinions, combined with the products and services offered by SVB are the basis for my view of the SPO. SVB serves emerging and middle-market growth companies in specific targeted niches. SVB is committed to its focus on technology and life science industries, while identifying and capitalizing on opportunities to serve other groups of clients with unique financial needs. SVB provides the majority of its clients with cash management, international trade, factoring, asset-based finance and other services designed to meet their changing needs as they progress through their business life cycle.

While the SPO is a choice worthy of consideration, I recognize that it is not the correct choice for every bank. So what bank is the SPO designed for? The first question each bank must ask is no surprise: "How will we fare under the standard Large Retail Bank test?" If your answer is clearly satisfactory or better, the SPO is not for your bank. No bank should go to the extra trouble and expense of preparing a strategic plan if its CRA record can stand on its own. How can you come to the conclusion that your bank's performance under the new examination procedures will be considered clearly satisfactory by your compliance examiner? Self evaluation against the

new procedures, that's how. An accurate self evaluation may be difficult, however, because the examination guidelines are new and untested, and because the guidelines provide as many questions as they do answers.

Performance under the Lending Test may be measured, at least in part, by analyzing the percentage of loans your bank has made in its assessment area (which may or may not be the same as your delineated community), including small business loans. This may be difficult for those banks that do not geo-code their non-HMDA reportable loans. Also, while most banks obtain revenue information during the commercial credit application process, many banks do not have a system that allows for easy evaluation of the revenue size of commercial loan clients. But once the geographic and revenue information is combined into one database, you will have all of the information required to measure past performance under the Lending Test and then, if needed, to develop measurable goals for a Strategic Plan. This information includes the number of loans made within your assessment area, the number of loans made in low-and moderate-income census tracts, and the number of small business loans your bank has made within and outside your assessment area. A bank can develop projections for the future by analyzing this data--projections that may serve as measurable goals for a Strategic Plan.

Although the new CRA is heavily weighted on lending performance, setting measurable goals under the Service and Investment Tests is also necessary if you choose the SPO. Measuring lending performance and setting goals by analyzing geographic and revenue data is possible but analyzing performance and setting goals under the Service and Investment criteria may prove more difficult. A key factor in measuring performance in these areas is the development of an accurate performance context for your institution. While the performance context of your institution will impact your entire examination, the value of your investments and services may be disproportionally affected by an inaccurate definition of your performance

context. Although the examiners must develop the context under which an institution will be evaluated, a bank may want to report additional information that the examiners need to know to properly evaluate the bank's performance. Examiner acceptance or consideration of the context you create for your institution may play a key role in your CRA rating and may help your bank gain approval of its Strategic Plan.

After conducting these analyses and developing a plan, a bank has two more obstacles to overcome: public scrutiny and regulatory approval. After developing a Plan and allowing for the consideration of public comment, there is no guarantee of regulatory approval. A recent article in the American Banker reported that eight banks had submitted Strategic Plans for regulatory approval to the FDIC or FRB, only to have them rejected for failing to set precise enough goals. This has discouraged other lenders from pursuing the SPO, especially considering the sensitivity around release of strategic information to their competitors. Providing the specificity of goals necessary to gain approval of a Plan could provide competitors with an edge that many banks are unwilling to allow.

A satisfactory CRA rating is important to banks for a variety of reasons, but especially for those with expansion or contraction plans, those that hope to participate, at any level, in the industry's current game of Pac Man and those interested in becoming active in interstate branching. While Silicon Valley Bank has not committed to the SPO, we believe that a full consideration of it, as well as other examination alternatives, is necessary to minimize the risk of regulatory intervention in our bank's business plans.