FEDERAL RESERVE BANK OF SAN FRANCISCO

Community Investments Vol. 10, Issue 4 Consortia and the CRA

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Fall 1998

Multi-bank community development organizations ("consortia") represent the industry's best effort to formalize community development lending as an equal partner in the world of traditional banking. By assuming the role of sub-contractor to their bank investors, consortia can provide the community development expertise and capacity that small- and mid-sized financial institutions cannot often afford. At the same time, these intermediaries can provide large financial institutions with an effective way to reach underserved populations through products and services that may initially be unprofitable if performed internally.

The role of consortia within the financial industry is still a topic for discussion in many banking circles, and regulatory agencies have no role in determining the mechanisms in which banks meet the credit needs of their communities. However, one role that the regulatory agencies do play is in setting the foundation for bank participation in newly formed consortia by providing regulatory guidance. The Federal Reserve Bank of San Francisco is currently providing such guidance to two-dozen financial institutions in the State of Utah that are undertaking the task of creating a statewide consortium. The grid presented on the following page is derived from a presentation delivered to these financial institutions in an effort to explain the CRA implications of consortia lending.

Setting the foundation for this grid are two over-arching issues concerning assessment area and the innovation/complexity of consortia products. The regulation clearly states that community development loans, services, and qualified investments are considered under CRA if they support a community development organization or activity that services an area which includes a financial institution's assessment area. The assessment area need not receive an immediate or direct benefit as long as the purpose, mandate, or function of the activity serves the geographies and/or individuals inside the assessment area or an area that is larger, but includes the assessment area. Keep in mind, however, that an examiner will consider community development activities that have a direct benefit to an institution's assessment area as being more responsive to the credit needs of that area than those activities whose benefit is uncertain or diffused throughout a larger area.

Another factor to take into consideration is the level of innovation and complexity. This is determined by a financial institution's efforts to meet community development needs not being met in the normal course of business by the local private market. Financing an organization such as a consortium that provides innovative and complex products and services is all well and good, and will likely result in the typical "garden variety" CRA consideration. But, active partnership with a consortium in the development, management, and distribution of such products and services will result in innovative and complex consideration under the CRA . . .the stuff of which Outstanding ratings are made.

Understanding the role of consortia, what they can and cannot do, and how to use multi-bank initiatives to provide the greatest impact to those most in need requires a partnership of resources and expertise. While the financial industry continues to evolve, the role of consortia must change with the industry in order to continue the mission of meeting the changing needs and expectations of bank investors. The four federal banking regulatory agencies are committed to assisting the industry in the development and evolution of multi-bank community development initiatives. And, while the CRA is challenging at times, it provides plenty of flexibility to try new things through intermediaries like consortia.

	Large Financial Institutions	Small Financial Institutions	Wholesale or Limited Financial Institutions
Lending	Lending Test: Loans made to a consortium are considered community development loans. Loans made through a consortium either through participation or purchase are also considered community development loans. The loans made by a consortium as a result of a financial institution's loans or investments will allow that	The focus of the streamlined CRA examination procedures for small financial institutions is on lending and lending-related activities. Loans made to a consortium are considered community development loans, as are loans made through a consortium either through participation or purchase. The loans made by a consortium as a	Community Development Lending: Similar to large financial institutions, loans made by wholesale and limited purpose financial institutions to a community development consortium are considered community development loans, as are loans through a consortium either through participation or purchase. The loans made by a

	financial institution to receive continuing consideration for community development lending activity as long as documentation supports this continued activity. For CRA reporting purposes, multi-family affordable housing loans are considered both a home mortgage and a community development loan.	result of a small financial institution’s loans or investments will allow that financial institution to receive continuing consideration for community development lending activity as long as documentation supports this continued activity. Participation in a consortium can also be an adjustment factor for a low loan-to-deposit ratio and allows for a bigger “bang for the buck” by providing access to innovative financing that would not be available if the	consortium as a result of a financial institution’s loans or investments will allow that financial institution to receive continuing consideration for community development lending activity as long as documentation supports this continued activity. For CRA reporting purposes, multi-family affordable housing loans are considered both a home mortgage and a community development loan.

		institution did not participate in the organization.	
Investments	Investment Test: Any lawful investment in a consortium, be it for creation, capitalization, or the purchase of securitized loans, is considered a qualified investment. In the cases where the consortium generates both community development loans and community development investments, the split credit rule may apply, allowing both lending and investment test consideration for the same tranaction. (See Community	The most recent Interagency Questions & Answers document on CRA clarifies that lending-related investments, such as an investment to capitalize or create a consortium, will be evaluated by examiners when evaluating small financial institutions for a satisfactory CRA rating under the streamlined examination procedure.	Community Development Investment: Any lawful investment in a consortium, be it for creation, capitalization, or the purchase of securitized loans, is considered a qualified investment. In the cases where the consortium generates both community development loans and community development investments, the split credit rule may apply, allowing both lending and investment test consideration for the same transaction. (See

	Investments, Winter and Spring 1997)		Community Investments, Spring 1996, and Spring 1997)
Services	Service Test: Participation by financial institution representatives in the provision of financial services-related activities to consortia is considered a community development service. This includes, but is not limited to: participation on the task force to create a consortium, participation on the organization's board of directors, and participation on the organization's loan committee.	The provision of community development services to the consortium will help a small financial institution if they choose to be evaluated for an Outstanding CRA rating.	Community Development Service: Formal participation by financial institution representatives in the provision of financial services-related activities to consortia is considered a community development service. This includes, but is not limited to: participation on the task force to create a consortium, participation on the organization's board of directors, and participation on the organization's loan committee.

About the Author

Fred Mendez is a community investment advisor for the Federal Reserve Bank of San Francisco, which he joined in 1993. In this role, he educates representatives of the financial and community development industries on the CRA, community and economic development, the secondary market, fair lending, and bank reform issues.

Fred came to the Federal Reserve from the investment banking industry and holds two degrees in Economics.