AL 97-2
Subject: Community Development Securities

TO: Chief Executive Officers of all National Banks, Community Development Finance Organizations, OCC Department and Division Heads, and All Examining Personnel

PURPOSE

In response to questions received from national banks, this advisory letter informs national banks of the standards that Community Development (CD) Securities must meet to qualify for purchase under the authority granted by the Investment Securities regulation, 12 CFR 1. It also explains the treatment of those investments under the Community Reinvestment Act regulation, 12 CFR 25.

DEFINITION

CD Securities are securities that are backed by interests in pools of community development loans, such as loans to borrowers in low- and moderate-income areas, or to small businesses. These securities typically are not rated by a nationally recognized statistical rating agency.

DISCUSSION

Twelve USC 24(Seventh), and its implementing regulation, 12 CFR 1, authorize national banks to purchase, sell, deal in, underwrite, and hold certain types of securities. Under the standards in part 1, a national bank may purchase and hold unrated CD Securities if the bank concludes, based on reliable estimates, "that the obligor will be able to satisfy its obligations under that security, and the bank believes that the security may be sold with reasonable promptness at a price that corresponds reasonably to its fair value." See 12 CFR 1.3(i). Acquisitions of CD Securities also must be consistent with safe and sound banking practices. Although CD Securities typically do not receive a rating from a nationally recognized statistical rating agency, part 1 permits national banks to invest in those securities if the bank documents that the issuer of the security will perform. See OCC Interpretive Letter No. 703. Performance documentation may be based on the bank's assessment of the project underlying the security, credit underwriting standards, or credit enhancements offered by the organization offering the securities to support the security and the quality of the underlying loan pools. Enhancements such as mortgage insurance, over collateralization of small business loans, the issuing organization's commitment to repurchase delinquent loans, and other enhancements also may demonstrate the obligor's ability to perform.

Under part 1, national banks may purchase securities acquired on the basis of reliable estimates including, but not limited to, CD Securities, in an aggregate amount no greater than 5 percent of their capital and surplus.

National banks may also purchase CD Securities as investments under the CDC, CD Project, and other Public Welfare Investments regulation, 12 CFR 24, if the CD Securities meet the public welfare requirements of part 24. See 12 CFR 24.3(a).

CRA CONSIDERATIONS

Under the CRA regulation, a national bank can receive positive consideration for making a "qualified investment" that benefits its assessment area(s) or a broader statewide or regional area that includes its assessment area(s). See 12 CFR 25.12(s). A bank's investment in CD Securities would be considered a qualified investment under the CRA regulation, provided the investment benefits the bank's assessment area(s) or a broader statewide or regional area that includes its assessment area(s). This is true even if the loans backing the security are not located within the bank's assessment area(s).

CONTACTS

If you have any questions about this advisory, please feel free to contact the Community Development Division at (202) 874-4930; the Community and Consumer Law Division at (202) 874-5750; or the Securities and Corporate Practice Division at (202) 874-5210.

Bert A. Otto
Assistant Deputy Comptroller
for Compliance Management
Date: February 25, 1997