Commercial Community Development Activities

Summary Conclusion: OTS may take no action positions on a case-by-case basis for community development investments that are consistent with the spirit and intent of HOLA § 5(c)(3)(A), even though the investments do not meet all of the technical requirements of that section, provided certain conditions are met.

Date: February 9, 2004

Subjects: Home Owners’ Loan Act/Savings Association Powers

P-2004-1
Re: Commercial Community Development Activities

Dear [ ]:

This responds to your recent letter submitted on behalf of [ ] ("Association"), a federal savings bank, requesting that the Office of Thrift Supervision ("OTS") confirm that it will not take action against the Association for violation of § 5(c)(3)(A) of the Home Owners’ Loan Act ("HOLA") \(^1\) if the Association acquires an interest in a limited partnership established to acquire, renovate, and reposition retail real estate in low- and moderate-income areas.

In brief, we conclude that the OTS will not take action against the Association for violation of § 5(c)(3)(A) of the HOLA if the Association makes the proposed investment, provided that certain conditions described herein are met.

I. Background

The Association’s home office and [ ] branch offices are located in [ ] Florida. The Association proposes to acquire a limited partnership interest in Community Reinvestment Partners, LP, a Delaware limited partnership ("Partnership"). The general partner of the Partnership is Community Reinvestment Partners, LLC, a Delaware limited liability company ("General Partner"). The Partnership will be managed by Community Reinvestment Advisors, LLC ("Manager").

You indicate that the Partnership will make investments in low- and moderate-income communities in the State of Florida as a qualified “community development entity.” In particular, the Partnership will focus primarily on acquiring, renovating, and repositioning grocery-anchored community centers, strip centers, and power centers throughout Florida’s major metropolitan areas. You indicate that all of the Partnership’s acquisitions are expected to be located in low and moderate-income census tracts in Florida. You note that Manager is an affiliate of Ram Realty Services, and that Ram “has a history of acquiring, renovating, leasing, and managing assets in low income communities in a way that both respects the community and protects its capital investments.”

You have provided a copy of the proposed Agreement of Limited Partnership of Community Reinvestment Partners, LP (“Partnership Agreement”). Section 1.6 of the Partnership Agreement indicates that the Partnership’s primary purpose is to make investments in low and moderate income communities intended to qualify for credit under the Community Reinvestment Act in the State of Florida as a qualified community development entity as provided in Section 45D of the [Internal Revenue Code of 1986, as amended], and the regulations promulgated thereunder, and thereby promoting economic revitalization, business development and job creation in such communities, . . .

You also note that the partnership has been approved as a statewide Community Development Entity (“CDE”) by the United States Department of the Treasury’s Community Development Financial Institutions Fund (“CDFI Fund”). As explained on the CDFI Fund’s Web site, “[i]n order to be certified as a CDE, an organization must be a legally established entity, have a primary mission of serving Low Income Communities or Low Income People and maintain accountability to residents of the Low Income Communities that it serves.” Under the CDFI Fund’s New Market Tax Credit Program,

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2 You indicate that acquisition opportunities are anticipated to be concentrated in the following major metropolitan areas: South Florida (Palm Beach, Miami-Dade and Broward counties), the Tampa Bay area (Pinellas, Hillsborough, and Polk counties); the Orlando area (Orange, Osceola, and Seminole counties); and the Jacksonville area (Duvall, Nassau, St. Johns, and Clay counties).

3 See the CDFI Fund’s List of Certified Community Development Entities as of December 31, 2003, located at www.cdfifund.gov.

4 Id. at “New Market Tax Credit Program: Overview” http://www.cdfifund.gov/programs/nmtc/.
taxpayers may receive a credit against Federal income taxes for making qualified equity investments in designated CDEs.\textsuperscript{5}

You indicate that the Partnership is seeking $150 million in equity, of which 3\% will be invested by the General Partner or its affiliates. The Association anticipates contributing a total of $[ ] to the Partnership, with an initial capital contribution of $[ ]. Finally, you state that the General Partner anticipates that “grocery-anchored neighborhood shopping centers” will be the Partnership’s general focus, and that most of the assets to be pursued by the Partnership are anticipated to be in underserved urban areas.

The OTS’s Southeast Regional Office has submitted material supporting your request and concurs in your belief that, although the Association’s proposed investment does not appear to meet all the technical requirements of the community development investment authorization in HOLA § 5(c)(3)(A), the proposed investment is consistent with the spirit and intent of that section. The Region has not identified any safety and soundness concerns, including loans to one borrower limitations, with the proposed investment.

II. Discussion

Section 5(c)(3)(A) of the HOLA authorizes federal savings associations to invest up to 2\% of their assets in equity investments in real estate located in “a geographic area or neighborhood receiving concentrated development assistance . . . under title I of the Housing and Community Development Act of 1974.”\textsuperscript{6} The principal program administered by the Department of Housing and Urban Development (“HUD”) under Title I is the Community Development Block Grant (“CDBG”) program.

As we have previously explained,\textsuperscript{7} when the provision that is now § 5(c)(3)(A) of the HOLA was enacted, the CDBG program encouraged localities to target Neighborhood Strategy Areas (“NSA”) to receive concentrated development assistance under Title I.\textsuperscript{8}

\textsuperscript{5} Id. See also “Notice of Allocation Availability (NOAA) Inviting Applications for the New Market Tax Credit Program,” 68 Fed. Reg. 42,806 (July 18, 2003).


\textsuperscript{8} 24 C.F.R. §§ 570.201(e) and 570.301(c) (1978).
Federal savings associations could thus easily determine what areas in their communities received “concentrated development assistance” and therefore qualified for § 5(c)(3)(A) investments by reviewing NSA designations. The CDBG program, however, no longer contains an NSA component. Under the current CDBG program, grants are given to CDBG entitlement communities (mostly cities of 50,000 or more), to the States for expenditure in a manner consistent with HUD guidelines, and to some smaller cities and local jurisdictions. Localities are no longer required or encouraged to concentrate their Title I funding in particular neighborhoods. Rather, Title I funds can be expended to support any project that: (1) is located in an entitlement community, a nonentitlement area that is covered by a CDBG program administered by a State, or a jurisdiction that participates in the Small Cities program, and (2) meets CDBG project requirements for benefiting low- and moderate-income persons or supporting certain other public welfare objectives.  

In an opinion dated May 10, 1995 (“1995 Opinion”), OTS observed that the reference in HOLA § 5(c)(3) to “concentrated development assistance” was obsolete. Rather than render the provision a nullity and frustrate its congressional purpose, OTS indicated it would take no-action positions for community development investments consistent with the spirit and intent of the statutory authority.

The 1995 Opinion also set out standards for community development investments in residential real estate, and specifically noted that a thrift may seek case-by-case no action positions from OTS for “other investments” that a thrift believes are “consistent with Title I and the HOLA.” Accordingly, OTS has reviewed particular proposed commercial real estate investments under the standards in the 1995 Opinion, with a slight modification of one standard. Pursuant to this case-by-case approach, OTS has taken no action positions with respect to specific commercial investments.

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10 In 1996, unrelated amendments to the HOLA affected the numbering of HOLA § 5(c)(3). The community development real estate provisions, which were formerly located at HOLA § 5(c)(3)(B), are now found at HOLA § 5(c)(3)(A).


Title I clearly encompasses commercial community development projects. Moreover, HOLA § 5(c)(3)(A) speaks in terms of “investments in real property and obligations secured by liens on real property,” language that includes commercial as well as residential real estate development projects. The issue, then, is whether the particular commercial investment that the Association desires to make is a bona fide community development investment, consistent with the spirit and intent of HOLA § 5(c)(3)(A) and Title I. We will review the Association's proposed investment under those standards set out in the 1995 Opinion, as modified for a nonresidential community development activity.

A. Location

The 1995 Opinion indicated that, at a minimum, a proposed investment must be located in an area eligible for Title I assistance. Thus, the investment must be located in either a CDBG entitlement community, in a nonentitlement community that has not been specifically excluded by the State in statewide submissions for CDBG funds, or in an area that participates in the Small Cities Program. The Opinion further noted that virtually all jurisdictions are covered by one of the foregoing designations.

Accordingly, as long as the projects in which the Partnership invests, acquires, or develops fall within such a community, as it appears they will, the location requirement would be met. Moreover, the Partnership’s designation as a CDE means that it must have a primary mission of serving low-income communities or low-income people, thereby providing even more assurance that the location requirement will be met.

B. Substantial Public Benefit

The subject of the May 1995 Opinion was a proposed residential investment, therefore, that Opinion required that the investment be made in a residential housing

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16 1995 Opinion at 3-4.

17 When federal savings associations invest in limited partnerships or corporations that make multiple equity investments in diverse locations, OTS will not object if the limited partnership or corporation invests no more than a de minimis amount of its funds in projects that are located in areas not eligible for Title I funding. OTS Op. Chief Counsel (November 22, 1996) at 5, n. 8. Investments will be deemed de minimis only if they do not exceed 10% of all investments made by the limited partnership or corporation. However, all investments in a limited partnership or corporation, even those covered by the de minimis rule, must meet each of the other standards. Id.
project that benefits low- and moderate-income people. However, as the Association proposes to invest in a Partnership that will invest in commercial projects, the 1995 Opinion’s specific requirement that the development be residential obviously does not apply. Instead, as we have done in the past, we will consider whether the proposed investment is consistent with the type of commercial projects that are eligible for funding under Title I.

The Title I regulations delineating the eligibility requirements for CDBG funding for specific community development projects are extremely complex. Even before the technical requirements of HOLA § 5(c)(3)(A) became obsolete, the provision was never read to require that a project meet all the HUD requirements to be eligible for investment by a federal thrift. Instead, it was read to permit investment in any project located in an area receiving concentrated Title I funding. In effect, the now obsolete concentration standard had served as a proxy for ensuring that the projects thrifts selected for investment would generally further the statutory community development objectives.

In the absence of the geographic concentration standard to screen potential investments, we believe it is appropriate to consider, and we have considered, whether a project is of the same general type as would be eligible for funding under Title I. In our view, to require a showing that a project meets all the precise details of the HUD regulations would cause § 5(c)(3)(A) to be more cumbersome and restrictive than Congress apparently intended.

Based on the information you have provided, including the stated purpose of the Partnership to make investments in low- and moderate-income communities; the Partnership’s designation as a CDE; and the fact that the Partnership’s Manager is an affiliate of an entity with a history of activities that benefit low income communities, it appears that the type of commercial projects of the Partnership would be generally consistent with the type of projects that are eligible for funding under Title I. Under these

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18 An individual or family will be deemed to be low-income when they earn less than 50% of the area median income. 12 C.F.R. § 563e.12(m)(1) (2003); cf. 24 C.F.R. §§ 91.5 and 570.3 (2003). An individual or family will be deemed to have a moderate income when they earn less than 80% of the median family income for the area. 12 C.F.R. § 563e.12(m)(2) (2003); cf. 24 C.F.R. §§ 91.5 and 570.3 (2003). As in the 1995 Opinion, we utilize OTS standards that closely approximate HUD Title I standards so as to minimize regulatory burden on thrifs. In each instance, the OTS standard is sufficiently similar to the HUD standard to serve the same policy purpose.

19 Based on our review of HUD's CDBG regulations, it appears that commercial real estate development projects can receive Title I funding if, inter alia, they either: (1) create or retain at least one full-time equivalent job per $25,000 of funds invested, or (2) provide goods and services to an area that has at least one low- or moderate-income person per $350 of funds invested. 24 C.F.R. § 570.209(b) (2003). Numerous other technical requirements are also imposed. See 24 C.F.R. Part 570, Subpart C (2003).

circumstances, we are satisfied that the Partnership will operate in a manner generally consistent with HUD’s public-benefit standards by providing retail services in low- and moderate-income communities, and by generating or preserving jobs in those communities.

C. Safety and Soundness

The 1995 Opinion also required that the investment be, under all the facts and circumstances, safe and sound. Although OTS has reviewed the proposed transaction, ultimate responsibility for ensuring that the investment is safe and sound lies with the Association. An association that makes an investment that is unsafe and unsound will not be shielded from supervisory or enforcement action merely because OTS reviewed the investment in advance.

D. Loans-to-One-Borrower Limitations

The 1995 Opinion also required, as a prudential matter, that the investment in a particular project or partnership not exceed an association’s loans-to-one-borrower limit set forth in OTS regulation § 560.93. As long as the Association’s investment in the Partnership does not exceed the applicable loans-to-one-borrower limit, the investment would not be objectionable on that basis.

E. Other Applicable Provisions of Law

The 1995 Opinion also required that the investment comply with all other applicable provisions of law, such as the investment limits in HOLA § 5(c)(3)(A), the capital requirements, and the requirements of OTS regulations. The Association should ensure that those requirements are satisfied.

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22 For these purposes, investments by a savings association in more than one limited partnership or corporation organized by the same non-profit organization or promoter will not be aggregated solely because there is a common organizer or promoter. We would reach a different conclusion, however, if the organizer or promoter guaranteed the investment or if the separate partnerships or corporations invested in the same project or projects.

23 Under OTS’s capital regulation, the Association’s investment may be placed in the 100% risk weight category if it would qualify as an equity investment permissible for a national bank. The Association should review 12 C.F.R. Part 24 (2003) to determine if the proposed investment would qualify as a permissible community development or public welfare investment for a national bank. 12 C.F.R. § 567.6(a)(1)(iv)(T) (2003). If it would not, then the investment must be deducted in calculating the Association’s total capital. 12 C.F.R. § 567.5(a)(2) (2003). In addition, the Association’s proposed investment in the Partnership would constitute a pass-through investment and would be subject to the limits set forth in OTS regulation 12 C.F.R. § 560.32 (2003).
Provided the conditions described herein are met, OTS will not object to the proposed investment by the Association. Prior to acquiring an interest in the Partnership, the Association should obtain written acknowledgment that the Partnership will observe the standards set forth in this opinion. The Association also should monitor the Partnership’s compliance with such standards and maintain records documenting compliance. OTS will review the documentation during periodic examinations.

In reaching the foregoing conclusions, we have relied upon the factual representations made in the material you provided to us, as summarized herein. Our conclusions depend upon the accuracy and completeness of those facts. Any material difference in facts or circumstances from those described herein could result in different conclusions. Moreover, this no action letter applies only to the specific transaction described herein. Because of the potential safety and soundness concerns presented by equity investments in commercial real estate, case-by-case OTS review will continue to be required for commercial investments under HOLA § 5(c)(3)(A), pending further notice.

If you have any further questions regarding this matter, please feel free to contact Vicki Hawkins-Jones, Special Counsel, at (202) 906-7034.

Sincerely,

Carolyn J. Buck
Chief Counsel

cc: All Regional Directors
    All Regional Counsel
    All Regional Community Development Liaisons