
**Office of the Comptroller of the Currency
Federal Deposit Insurance Corporation
Federal Reserve Board
Office of Thrift Supervision**

Interpretive Letter 709 (Revised)

July 1996

12 U.S.C. 2901

June 14, 1996

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Dear []:

This letter replaces our letter dated February 21, 1996, which responded to your request for clarification about the extent to which an institution that invests in a Community Development Bank (CDB) may obtain positive consideration under the lending test portion of the Community Reinvestment Act (CRA) regulations published May 4, 1995. See 60 Fed. Reg. 22,156 (May 4, 1995). Staff from all four of the financial institution regulatory agencies have reconsidered the issues you raised, and they concur in the opinions expressed in this letter.¹ As discussed below, an institution that invests in a CDB may obtain favorable consideration under the regulation's investment test, or it may choose to have a portion of its investment evaluated under the lending test and the remainder evaluated under the investment test.²

¹ This letter supersedes the February 21, 1996, letter in its entirety. Because this letter replaces the previous letter, we have substantially reiterated herein the portions of the previous letter that remain valid (with some minor edits for clarity). This letter contains a revised formula for determining the amount of community development loans made by a CDB in which a financial institution has invested for which the institution may receive consideration under the lending test.

² This letter addresses only CRA consideration for an investment in a CDB. It assumes that such an investment is legally authorized; however, it does not authorize such an investment. In a separate letter dated February 1, 1996, the OCC approved a national bank's investment in the CDB as a community development investment under 12 U.S.C. § 24

The CRA was designed to encourage institutions to help meet the credit needs of their entire communities, including low- and moderate-income areas, consistent with safe and sound lending practices. The new regulations set out a number of different tests for examiners to use in evaluating CRA performance, depending on the type of activity and the size and type of institution. Your letter focuses on whether institutions' investments in the CDB will receive positive consideration under the lending and investment tests. Our response, therefore, addresses consideration under the lending and investment tests, which are applicable primarily to large institutions.

The lending test evaluates an institution's lending activities by considering the institution's purchase or origination of home mortgage, small business, small farm, community development, and, in some instances, consumer loans. Among the performance criteria considered in the lending test is an institution's community development lending, including the number and amount of community development loans and their complexity and innovativeness. See 12 C.F.R. §§ 25.22(b)(4), 228.22(b)(4), 345.22(b)(4), and 563e.22(b)(4). A "community development loan" must have community development as its primary purpose and, except in the case of wholesale or limited purpose banks, must benefit the institution's assessment area(s) or a broader statewide or regional area that includes the institution's assessment area(s). See 12 C.F.R. §§ 25.12(i)(1) & (2)(ii), 228.12(i)(1) & (2)(ii), 345.12(i)(1) & (2)(ii), and 563e.12(h)(1) & (2)(ii). The regulation allows an institution that invests in a community development financial institution, such as a CDB, or other entity that uses the institution's investment to make loans to receive consideration under the lending test for its pro rata share of community development loans made by the entity. See 12 C.F.R. §§ 25.22(d), 228.22(d), 345.22(d), and 563e.22(d).

The investment test evaluates an institution's number and amount of qualified investments, the innovativeness or complexity of its qualified investments, the responsiveness of the qualified investments to credit and community development needs, and the degree to which the qualified investments are not routinely provided by private investors. See 12 C.F.R. §§ 25.23(e), 228.23(e), 345.23(e), and 563e.23(e). Qualified investments include lawful investments, deposits, membership shares or grants that have as their primary purpose community development. See 12 C.F.R. §§ 25.12(s), 228.12(s), 345.12(s), and 563e.12(r). To be considered under the investment test, qualified investments must benefit the institution's assessment area(s) or a broader statewide or regional area that includes the institution's assessment area(s). See 12 C.F.R. §§ 25.23(a), 228.23(a), 345.23(a), and 563e.23(a). Qualified investments include, but are not limited to, investments in CDBs that primarily lend in

(Eleventh) and 12 C.F.R. part 24.

low- and moderate-income areas or to low- and moderate-income individuals to promote community development and investments in state and municipal obligations that specifically support community development. See 60 Fed. Reg. at 22,162 n.3.

As noted above, an institution may choose to have its investment evaluated entirely under the investment test, or it may choose to have a portion of its investment evaluated under the lending test and a portion evaluated under the investment test. However, in doing so, the institution must provide the appropriate supervisory agency with the necessary information to calculate the breakdown between the two components.

An example may help to illustrate how an institution's investment in a CDB may be considered under the CRA regulations. Assume an institution invests \$1 million in a CDB that has a total capitalization of \$10 million. The CDB, in turn, holds total assets of \$30 million, with \$12 million in qualified investments and \$18 million in community development loans. The investing institution could choose to have its investment considered only under the investment test. If the institution chooses this option, the amount of the qualified investment would be \$1 million, the total amount of the institution's investment.

Alternatively, the investing institution could request consideration under both the investment and lending tests. The amount attributed to the investment test would equal the product of the institution's investment in the CDB and the percentage of the CDB's asset portfolio that is comprised of qualified investments. The amount attributed to the lending test would equal the investing institution's pro rata share of community development loans originated by the CDB during the period under review.

Applying these principles to the example above may help to clarify how an institution's investment in a CDB may be attributed between the investment and lending tests. In the example, qualified investments comprise 40 percent of the CDB's total assets (\$12 million of total assets of \$30 million). Thus, under the investment test, the investing institution would receive consideration of 40 percent of its total investment in the CDB, or \$400,000. It is assumed that the remainder of the institution's investment has been used to fund community development loans in an amount equal to the institution's pro rata share of loans originated by the CDB. The institution has supplied ten percent of the capital of the CDB, which provides the basis for determining, under the lending test, the institution's pro rata share of community development loans made by the CDB. Assuming the CDB's \$18 million in loans were originated during the period under review and benefit the institution's assessment area(s) or a broader statewide or regional area that includes the institution's assessment area(s), the

institution's pro rata share of these loans would be \$1.8 million. Therefore, the institution may receive consideration for \$1.8 million in community development loans under the lending test.

I trust this letter is responsive to your inquiry. You may also be interested to know that the staffs of the four financial supervisory agencies are presently developing official guidance for the public to aid in resolving interpretive questions arising under the new CRA regulations. In the meantime, if you have further questions, please feel free to call me or Margaret Hesse, an attorney on my staff, at (202) 874-5750.

Sincerely yours,

\s\

Matthew Roberts
Director
Community and Consumer Law Division
Office of the Comptroller of the Currency