The Office of the Comptroller of the Currency (OCC), Board of Governors of the Federal Reserve System (Board) and the Federal Deposit Insurance Corporation (FDIC) (collectively the Agencies) adopted as final the Interagency Questions & Answers (Q&As) regarding community reinvestment that were proposed on March 18, 2013. These Q&As continue the apparently never-ending process of policy tweaking and further adjustment by the Agencies to better align the aspirations of the Community Reinvestment Act (CRA) with the practical difficulties that sometimes constrain banks in the marketplace from being able consistently to meet the CRA requirements. Most of the new Q&As are not likely to spark great controversy, but several do represent restatements of the Agencies’ views, especially regarding qualified investments. The new Q&As became effective on November 20, 2013. The rules are not limited to only having prospective effect, and certain critical issues were deferred until examination procedures are written, and exams conducted. A link to the Q&As can be found at http://www.gpo.gov/fdsys/pkg/FR-2013-11-20/pdf/2013-27738.pdf.

The Q&As consist of five revised Q&As; two new Q&As; and one redesignated Q&A, without substantive change. The Q&As were first published in 1996 and were last revised by the Agencies on March 11, 2010.

In the Q&As, the Agencies made the following revisions:

1. With respect to clarifying community development activities outside an Institution’s Assessment Area(s) in the Broader Statewide or Regional Area that includes the Institution’s Assessment Area(s), the Agencies went to great lengths to streamline the language in the prior Q&A and simplify the operating rule to be that “examiners will consider [community development activities] even if they will not benefit the bank’s assessment area(s), as long as the institution has been responsive to community needs and opportunities in its assessment area(s),” Q&A §____12(h) – 6. In short, this means that a bank can conduct community development activities on a regional or statewide basis that includes its assessment area, in order to receive CRA “credit,” but the activity does not need to directly benefit the bank’s assessment area if the bank is otherwise responsive to community needs in its assessment area(s).

2. In a separate but related revised Q&A, the Agencies clarified that ‘a regional area’ may be an intrastate area or a multistate area that includes the financial institution’s assessment area(s). Regional areas typically have some geographic, demographic, and/or economic interdependencies and may conform to commonly accepted delineations, such as the ‘tri-county area’ or the mid-Atlantic states.” Q&A §____12(h) – 7. The Agencies made clear that the areas listed in the Q&A were not intended to be an exhaustive list or to otherwise serve as a limitation. Instead, the Agencies noted their intent to provide greater flexibility with the Q&A.

3. With respect to investments in nationwide funds, under the prior Q&As, the proposed Q&As and as clarified in the Q&As, banking institutions are authorized to invest in nationwide funds that include investments for low-
and moderate-income communities and underserved communities. In a somewhat circuitous comment review process, the Q&As now confirm that a bank may obtain CRA-qualified investment test credit for investments made in a nationwide fund that benefits the bank’s assessment area(s) as well as the broader statewide or regional area that includes the bank’s assessment area(s), provided, as previously noted above, that the bank is otherwise responsive to community needs in its assessment area(s). Q&A §__.12(h) – 6.

What the Q&As do eliminate is the prior guidance regarding written documentation about earmarking and side letters to allocate the underlying investments to the various multiple investors in a fund. In their comments to Q&A §__.23(a) – 2, the Agencies stated that they “do not intend the absence of such language to mean that side letters and earmarking are no longer permissible, but a side letter or earmarking documentation is not required in order to obtain CRA consideration.” The Agencies, however, noted that “few commenters offered suggestions as to how regulators should avoid double counting when considering nationwide investments.” Unfortunately, the Q&As indicate that the Agency examination procedures, rather than the regulatory rules, will be revised to address investments in nationwide funds and will address how to avoid double counting the same investment by multiple bank investors.

4. With respect to Community Services Targeted to Low- or Moderate-Income Individuals, the Agencies adopted the two proposed determinations related to: (1) students or their families from a school at which the majority of students qualify for free or reduced-price meals; and (2) individuals who receive or are eligible to receive Medicaid. After considering the comments received, the Agencies added another determination of community service to low- or moderate-income populations, for (3) recipients of government assistance programs that have income qualifications equivalent to, or stricter than, the definitions of low and moderate income defined by the CRA regulations. Q&A §__.12(g)(2) – 1. Examples include: the U.S. Department of Housing and Urban Development’s Section 8, 202, 515, and 811 programs; and the U.S. Department of Agriculture’s Section 514, 516, and Supplemental Nutrition Assistance programs. None of these determinations appeared to be controversial as part of the rulemaking process.

5. With respect to Service on the Board of Directors of an Organization Engaged in Community Development Activities, Q&A §__.12(i)–3 is revised to explicitly state that service on the board of directors of a community development organization is a technical assistance activity that would receive consideration as a community development service. Although the Q&A does not expressly state so, the comments indicate that such service is expected to provide genuine benefit to the institutions’ communities for consideration in a CRA evaluation, and mere attendance of board meetings, without more, would not suffice. Additionally, the Q&A added another explicit example of technical assistance activities eligible for CRA consideration: providing services reflecting financial institution employees’ areas of expertise at the institution, such as human resources, information technology, and legal services.

The Agencies also proposed two new Q&As: one addressed the treatment of community development lending performance in determining a large institution’s lending test rating and the other addressed the quantitative consideration given to a certain type of community development investment.

The Agencies also adopted two new proposed Q&As, as follows:

1. With respect to Community Development Lending in the Lending Test Applicable to Large Institutions, the Agencies proposed new Q&A §__.22(b)(4) – 2 to promote consistent treatment of community development lending among the Agencies and to clarify that community development lending performance is always a factor that is considered in a large institution’s lending test rating. The new Q&A further clarified that an institution’s record of making community development loans may have a positive, neutral, or negative impact on an institution’s lending test rating. The Agencies also reiterated an existing concept that strong performance in retail lending may compensate for weak performance in community development lending and, conversely, strong community
development lending may compensate for weak retail lending performance. The Agencies further clarified that community development lending is not mandated in all of a bank’s assessment areas. In their comments to Q&A §__.22(b)(4) – 2, the Agencies were explicit that “[e]xaminers will consider the absence or lack of community development lending in a particular assessment area within the context of the environment in which the institution operated during the evaluation period, including economic, demographic, and competitive factors, the institution’s financial capacity or constraints, and community needs and opportunities to make community development loans in the assessment area(s).”

2. With respect to Qualified Investments, Q&A §__.12(t) – 9 provides that examiners will give positive CRA consideration to investments that are made to organizations that have a primary purpose of community development. If an institution invests in an organization that in turn invests the received funds in instruments that do not have a primary purpose of community development and uses only the income from such instruments for community development, then the examiners will give consideration to only the amount of investment income that has a community development purpose. By contrast, if the organization invests in such an instrument to secure capital for leveraging purposes, to secure additional financing, or to generate a return with minimal risk until funds can be deployed toward an intended community development activity, then examiners will provide positive consideration for the total amount of such instruments, as well as for the related investment income.

3. With respect to the redesignation of an existing Q&A, without substantive change, in 2010, the Agencies revised their regulations to implement Section 804(b) of the CRA, addressing CRA consideration of majority-owned institutions’ activities with minority- and women-owned financial institutions and low-income credit unions (MWLICU). Q&A §__.12(g) – 4, which was adopted prior to the 2010 regulations implementation, is now redesignated as Q&A §__.21(f) – 1 to correlate to the 2010 regulatory provision addressing MWLICU issues. No substantive changes have been made to this Q&A.

**Pepper Points**

The adoption of the Q&As has been closely watched, receiving approximately 200 comments from private parties, including represented financial institutions and their trade associations, community development advocates and organizations, state bank supervisors, and others. The Q&As are intended to supplement the guidance released in 2010. Except where a 2010 Q&A is explicitly amended by a 2013 Q&A, the 2010 guidance remains in full force and effect. However, nothing in the Q&As indicates that the new Q&As will have prospective effect only, which means that existing investment arrangements, and other community development activities, could come under examiner scrutiny, including by using new standards to be issued as part of the examination procedures.

The new Q&As do not provide guidance on certain issues related to classifying qualified investments, especially investments in nationwide funds. The questions of how to attribute funds to an institution’s various assessment areas, or how regulators should avoid double counting when considering nationwide investments, were left to be resolved through examination procedures. It is alarming that these important issues were left unaddressed by the Q&As, as examination procedures can change, are not subject to comment, and can create less certainty and predictability for institutions wishing to comply with CRA.

In response to the Agencies’ request about comments on nationwide funds, some commenters proposed that the Agencies create a distinct “national needs” category for nationwide funds, allowing institutions to get consideration for general nationwide investment. The Agencies decided not to create a separate category for investments in nationwide funds. We agree. Creating such a new category would further complicate CRA examinations.

**Endnote**