INDEPENDENT COMMUNITY BANKERS *of* AMERICA®

June 14, 2022

Community Reinvestment Act (CRA): Summary of the 2022 Interagency Proposed Rule[1]

Introduction

The Community Reinvestment Act ("CRA")[2] was enacted in 1977 to combat redlining by ensuring that each insured depository institution serves the convenience and needs of its entire community, including low- and moderate-income (LMI) neighborhoods, consistent with its safe and sound operation.

The CRA has been amended several times since its original enactment, and its implementing regulations have changed as well, with the last major overhaul being completed in 1995. Since 2017, the Office of the Comptroller of the Currency (OCC), the Federal Deposit Insurance Corporation (FDIC) and the Federal Reserve Board of Governors (FRB) have worked to modernize the 1995 rule.

On May 5, 2022, the OCC, FDIC, and FRB released a proposed CRA rule that would create a modernized rule for the banking industry. Comments in response to the agency's notice of proposed rulemaking (NPR) are due on Aug. 5, 2022.[3] ICBA will submit a comment letter on behalf of the nation's community banks, but we encourage all community bankers to submit individual comments to the agencies detailing how the proposed rule will impact their bank.

The contents of the interagency proposal are summarized below.

Asset Thresholds

A key issue for community banks is whether they are classified as small banks, intermediate small banks (ISBs), or large banks. These size categories determine the complexity of the test that regulators will use to evaluate the bank's performance.

As advocated by ICBA, the proposed rule raises the current asset thresholds. A pillar of ICBA's advocacy has been that asset thresholds should be increased to reflect changes in the banking industry and the regulatory burden to which banks are already subject.

- **Small Bank —** The proposed small bank threshold **is $600 million**, a 73.41% increase from its current level of **$346 million.**
- **Intermediate Small Bank —** The proposed ISB threshold is **$2 billion**, a 44.51% increase from its current level of **$1.384 billion**.
- **Large Banks —** Large banks with assets exceeding **$10 billion** would be subject to evaluation of digital and other delivery systems and deposit products and other additional requirements.

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[1] Portions of this summary, including tables and formulas, are taken directly from the Notice of Proposed Rulemaking promulgated by the Office of the Comptroller of the Currency, the Federal Deposit Insurance Corporation, and the Federal Reserve Board of Governors, available at: https://www.regulations.gov/document/OCC-2022-0002-0001.

[2] 12 U.S.C. 2901 *et. seq.*

[3] 87 Fed. Reg. 33884.

Small and Intermediate Small Bank Opt-In

While a more transparent method of evaluating banks is a desirable goal, an incremental improvement in regulatory clarity may not be sufficient to justify requiring small banks and ISBs to completely overhaul their compliance management systems and retrain staff to comply with new requirements. Therefore, ICBA has argued that small banks and ISBs should have the option to opt-in any new CRA evaluation framework or continue to be evaluated under the status quo retail lending and community development tests.

In the new proposal, **ISBs would be evaluated under the new Retail Lending Test and the status quo community development test, unless they choose to opt into the new Community Development Financing Test. Small banks would be evaluated under the status quo small bank lending test, unless they choose to opt into the new Retail Lending Test.** In other words, for banks below $600 million in assets, the existing small bank Lending Test would remain the default method of evaluation. Banks between $600 million and $2 billion in assets would be required to comply with the new Retail Lending Test but would have the option to retain the current community development test.

Banks with assets exceeding $2 billion would be required to comply with the new tests and would not have the option to retain their current exam framework.

New Assessment Area Rules

The current CRA rule requires banks to delineate assessment areas in geographies where their bank has a physical branch presence. According to the proposal, "facility-based assessment areas would remain a cornerstone of the proposed evaluation framework." As is the case in the current rule, assessment areas may not reflect illegal discrimination or arbitrarily exclude low- or moderate-income census tracts.

Small banks and ISBs would continue to be allowed to delineate assessment areas including the portion of a county that the bank can be reasonably expected to serve, provided they continue to include only whole census tracts. However, large banks would be required to delineate assessment areas that "consist of one or more MSAs or metropolitan divisions or one or more contiguous counties within an MSA, a metropolitan division, or the nonmetropolitan area of a state." In other words, large banks would no longer be permitted to delineate portions of a county as a facility-based assessment area.

Large banks, in addition to facility-based assessment areas, would be required to delineate new retail lending assessment areas in geographies where they have a concentration of retail loan originations outside of their facility-based assessment areas. Only the Retail Lending Test would be applied in these assessment areas. These new assessment areas would consist of either:

(i) The entirety of a single MSA excluding counties inside their facility-based assessment areas; or

(ii) All of the nonmetropolitan counties in a single state, excluding counties inside their facility-based assessment areas, aggregated into a single retail lending assessment area.

The delineation of a retail lending assessment area would be required in any MSA or the combined non-MSA areas of a state, respectively, in which a bank originated in that geographic area, as of Dec. 31 of each of the two preceding calendar years:

(i) at least 100 home mortgage loans outside of its facility-based assessment areas; or
(ii) at least 250 small business loans outside of its facility-based assessment areas.

The agencies estimate that, using these thresholds, 104 large banks will be required to delineate at least one retail lending assessment area in a geography where they lack a physical branch. This proposed change will likely expand the number of geographic areas where branchless, internet-based banks are evaluated. However, as the agency estimates show, it will also likely impact some traditional, branch-based banks.

Out of Area Activities — Finally, as advocated by ICBA, the agencies' proposal grants credit for qualifying community development financing and services activities conducted beyond the boundaries of a bank's facility-based assessment areas. According to the proposal, banks "would receive consideration for qualifying activities anywhere in a state or multistate MSA in which they maintain a facility-based assessment area, when determining the conclusion for that state or multistate MSA. In addition, banks would receive consideration at the institution level for any qualifying activities conducted nationwide." This broader geographic consideration of CD financing will ensure that banks receive credit for the beneficial community development loans and investments they make outside the confines of their assessment areas.

Qualifying Activities Confirmation and Illustrative List of Activities

The proposal would require the agencies to maintain **a publicly available illustrative, non-exhaustive list of activities eligible for CRA consideration.** The agencies also propose including a process for modifying the illustrative list of activities periodically. **In addition, the agencies are proposing a process, open to banks, for confirming eligibility of qualifying community development activities.** In this process, banks would submit the details of a potential loan or investment to their regulator and could receive a binding decision about whether the loan or investment would be eligible for CRA credit.

Impact Review of Community Development Activities

The agencies propose to conduct an impact review of community development activities under the Community Development Financing Test, the Community Development Financing Test for Wholesale or Limited Purpose Banks, and the Community Development Services Test. The impact review would qualitatively evaluate the impact and responsiveness of qualifying activities with respect to community credit needs and opportunities.

To achieve this, the agencies would consider whether a loan or investment should be given additional credit based on several impact factors. These factors include:

1. Activities Serving Persistent Poverty Counties and Geographies with Low Levels of Community Development Financing.
2. Activities Supporting MDIs, WDIs, LICUs, and Treasury Department-Certified CDFIs.

3. Activities Serving Low-Income Individuals.
4. Activities that Support Small Businesses or Farms with Gross Annual Revenues of $250,000 or Less.
5. Activities that Support Affordable Housing in High Opportunity Areas.
6. Activities Benefitting Native Communities.
7. Activities that Are a Qualifying Grant or Contribution.
8. Activities that Reflect Bank Leadership through Multi-Faceted or Instrumental Support.
9. Activities that Result in a New Community Development Financing Product or Service.

Performance Tests, Standards, and Ratings

Small Banks — Small banks will be evaluated under the current lending test as the default evaluation method. However, small banks would have the ability to opt into the proposed Retail Lending Test.

Intermediate Banks — The agencies would evaluate ISBs under the new Retail Lending Test and the current intermediate small bank community development test or, at the bank's option, under the proposed Community Development Financing Test. Certain features of the Retail Lending Test and Community Development Financing Test would be tailored for intermediate banks, including by maintaining current data collection, maintenance, and reporting requirements for intermediate banks that do not elect to be evaluated under the new Community Development Financing Test.

Large Banks — Large banks would be subject to four performance tests for large banks: a Retail Lending Test, a Retail Services and Products Test, a Community Development Financing Test, and a Community Development Services Test.

Banks Over $10 billion — Banks over $10 billion would have additional requirements for deposits data, retail services data on digital delivery systems, retail services data on responsive deposit products, and community development services data. In addition, the agencies propose that banks with assets over $10 billion, including wholesale and limited-purpose banks, would have automobile lending data requirements.

Strategic Plan — Banks would retain their ability to be evaluated under a strategic plan.

Ratings — The agencies would assign ratings on each performance test in facility-based assessment areas, states, multistate MSAs, and at the institution level. Ratings would be either "Outstanding," "High Satisfactory," "Low Satisfactory," "Needs to Improve," and "Substantial Noncompliance."

Large Banks, ISBs, and Small Banks That Opt In: Retail Lending Test

The proposed Retail Lending Test would apply to large banks and ISBs and to small banks that choose to opt in. It would be applied in each of several major product lines:

- **Closed-end home mortgage loans —** all closed-end home mortgage loans secured by a one-to-four-unit dwelling.

- **Open-end home mortgage loans —** all open-end home mortgage loans secured by a one-to-four-unit dwelling.
- **Multifamily loans —** loans secured by multifamily housing will be considered as a major product line. The proposal also considers the subset of multifamily loans that provide affordable housing to low- or moderate-income individuals under the Community Development Financing Test.
- **Small business loans —** the agencies propose to define "small business" and "small farm" in the CRA regulations in alignment with the CFPB's proposed definition of "small business" in its Section 1071 Rulemaking. As such, the agencies propose to define "small business" as a business having **gross annual revenues of $5 million or less** for its preceding fiscal year. This is a significant increase from the current level of $1 million.
- **Small farm loans —** a small farm loan would be a loan to a farm with gross annual revenues of $5 million or less.
- **Automobile loans —** automobile loans will be evaluated for banks with $10 billion or more in assets. Auto loans are the only type of consumer loan to be quantitatively evaluated under the proposed rule's framework.

Purchased Retail Loans — On the Retail Lending Test, examiners would count an examined bank's purchased retail loans as equivalent to its retail loan originations. The agencies acknowledge the important role of loan purchases in providing liquidity BUT leave open the possibility of adjusting a retail lending conclusion in which an examiner determines that loan purchases reflect loan churning, after conducting the retail lending volume and distribution analyses.

Credit Card Loans and Other Consumer Loan Categories — The agencies propose to evaluate other consumer loan categories, including credit cards, qualitatively under the Retail Services and Products Test. Under this approach, examiners would review the responsiveness of these credit products by considering the number of low- and moderate-income customers using each selected product and how they use the product, including rates of successful repayment under the original loan terms. Other aspects of responsiveness could include the loan terms, underwriting, pricing, and safeguards that minimize adverse borrower outcomes.

Overview of Proposed Retail Lending Test Approach — The new test will use metrics and performance standards to evaluate a bank's lending to low- and moderate-income borrowers, small businesses and small farms, and low- and moderate-income neighborhoods in its assessment areas. The agencies propose two sets of metrics: the retail lending volume screen and a series of distribution metrics.

The Retail Lending Volume Screen would assess a bank's volume of retail lending relative to its deposit base, compared to other banks in each facility-based assessment area. The distribution metrics and dynamic thresholds would be used to individually evaluate each of a bank's major product lines, in each facility-based assessment area, and, as applicable, in each retail lending assessment area and outside retail lending area.

<u>Retail Lending Test: Volume Screen</u>

The market volume benchmark would measure the average annual dollar amount of retail originations in the assessment area by all large banks that operate a branch in the assessment area in the numerator, divided by the annual average amount of deposits collected by those same banks from that assessment area in the denominator. Under the proposal, banks would pass the retail lending volume screen with a bank volume metric of at least 30 percent of the market volume benchmark. If a bank meets or exceeds this threshold, the agencies would evaluate the bank's major product lines under the distribution metrics approach.

$$\frac{\text{average annual dollar amount of retail originations in the assessment area by all large banks that operate a branch in the assessment area}}{\text{average amount of deposits collected by those same banks from that assessment area}} = X$$

Your bank is eligible to be evaluated using the distribution metrics if:

$$\frac{\text{Your bank's retail lending originations by dollar amount in an assessment area}}{\text{Your bank's deposits collected from an assessment area (Using FDIC SOD data)}} = 0.30(X)$$

Retail Lending Test: Bank Geographic Distribution Metrics and Borrower Distribution Metrics

The geographic distribution metrics measure the level of bank lending in low-income and moderate-income census tracts in an assessment area. The borrower distribution metrics measure the level of lending to low-income borrowers, moderate-income borrowers, small businesses or small farms with gross annual revenues of $250,000 or less, and small businesses or small farms with gross annual revenues greater than $250,000 but less than or equal to $1 million, depending on the product line being evaluated. Bank lending is compared to these benchmarks.

To calculate these distribution metrics, the agencies propose using the number of a bank's loans, not the dollar amount of those loans. For example, under the proposed approach, one $250,000 home mortgage would count the same as one $80,000 home mortgage.

The agencies propose using two **geographic distribution components/metrics for each product line**:

- Loans in low-income census tracts.
- Loans in moderate-income census tracts.

The metric would measure the number of a bank's loans located in low-income and moderate-income census tracts, respectively, relative to the total number of the bank's loans in the assessment area. An example is provided below

$$\frac{\textit{Bank Loans in Low-Income Tracts}\ (5)}{\textit{Bank Loans}\ (25)} = \textit{Geographic Bank Metric}\ (20\%)$$

With the exception of multifamily lending, the agencies propose using **two borrower distribution components for each product line.**

For closed-end home mortgage loans, open-end home mortgage loans, and automobile lending, the two borrower distribution components would be:

- Loans to low-income borrowers.
- Loans to moderate-income borrowers.

For small businesses, the two borrower distribution components would be:

- Loans to small businesses with gross annual revenues of $250,000 or less.
- Loans to small businesses with gross annual revenues above $250,000 and less than or equal to $1 million.

For small farms, the two borrower distribution components would be:

- Loans to small farms with gross annual revenues of $250,000 or less.
- Loans to small farms with gross annual revenues above $250,000 and less than or equal to $1 million.

For example, if Bank A originated 100 total closed-end home mortgage loans in an assessment area, and made 20 of those loans to low-income borrowers, it has a low-income borrower bank metric of 0.2 because 20 percent of its total loans were made to low-income borrowers.

$$\frac{\textit{Bank Loans to Low–Income Borrowers}\ (20)}{\textit{Bank Loans}\ (100)} = \textit{Borrower Bank Metric}\ (20\%)$$

<u>Retail Lending Test: Thresholds</u>

The metrics calculated using the steps above would be compared to **thresholds** using the following scale to establish presumptive ratings:

The thresholds would be calculated using local data to tailor exams to the specific assessment area that a bank lends in. There will be a community benchmark, which looks at community demographics, and a market benchmark that examines the performance of peer lenders.

For example, in the multifamily product line, the community benchmark would compare bank lending to the "percentage of multifamily units in low-income census tracts or moderate-income census tracts as applicable, in assessment area." The market benchmark would compare bank performance to the percentage of “multifamily mortgages in low-income census tracts or moderate-income census tracts in assessment area, as applicable, by all lender reporters.”

Details about the benchmarks for other product lines can be found in the NPR.

Distribution Metric		Community Benchmark	Market Benchmark
Multifamily			
Geographic Distribution Metric	**Data Point**	Percentage of multifamily units in low-income census tracts or moderate-income census tracts as applicable, in assessment area	Percentage of multifamily mortgages in low-income census tracts or moderate-income census tracts in assessment area, as applicable, by all lender-reporters
	Data Source	American Community Survey (Census)	HMDA Data

To establish presumptive ratings, examiners would expect the following levels of performance when bank lending is compared to the relevant benchmark:

- **33 percent** of the market benchmark and **33 percent** of the community benchmark are intended to reflect performance expectations for the “**Needs to Improve” threshold.**
- **80 percent** of the market benchmark and **65 percent** of the community benchmark are intended to reflect performance expectations for the “**Low Satisfactory” threshold.**
- **110 percent** of the market benchmark and **90 percent** of the community benchmark are intended to reflect performance expectations for the **“High Satisfactory” threshold.**
- **125 percent** of the market benchmark and **100 percent** of the community benchmark are intended to reflect performance expectations for the **“Outstanding” threshold.**

Large Banks: Retail Services and Products Test

The Retail Services and Products test would evaluate large banks’: (i) delivery systems; and (ii) credit and deposit products responsive to low- and moderate-income communities’ needs. It would use a predominately qualitative approach while incorporating quantitative measures as guidelines.

This test would primarily evaluate branch distribution and the ability of low- and moderate-income customers to access bank branches. Additional services evaluated would include:

- Extended business hours, including weekends, evenings, or by appointment.

- Providing bilingual/translation services.
- Free or low-cost check cashing services, including government and payroll check cashing services.
- Reasonably priced international remittance services.
- Electronic benefit transfer accounts.

Large Banks and ISBs That Opt In: Community Development Financing Test

The new Community Development Financing Test would apply to large banks and any intermediate bank that opts into it. The test will consist of a community development financing metric and benchmarks and an impact review. It would be applied at the facility-based assessment area, state, multistate MSA, and institution levels. It would not be assessed for retail lending assessment areas.

The bank community development financing metrics would measure the dollar value of a bank's community development loans and community development investments together, relative to the bank's capacity, as reflected by the dollar value of deposits. This is a change from the current approach for large banks, which evaluates loans and investments separately.

The impact review would evaluate the impact and responsiveness of a bank's community development loan and community development investment activities through the application of the factors discussed in the section titled "Impact Review of Community Development Activities." This analysis would provide additional recognition for activities that, while relatively small in dollar value, are particularly responsive to community needs.

Within an assessment area, a bank's financing metric would be the ratio of its community development financing dollars (the numerator) relative to the dollar value of the deposits (the denominator). In the following example, a bank made $20,000 of community development loans and investments in an assessment area where it took $1 million in deposits. Therefore, its CD financing metric in that assessment area is 2%.

$$\frac{\textit{CD loans}+\textit{CD investments}\ (\$20{,}000)}{\textit{deposits}\ (\$1{,}000{,}000)} =$$

Bank Assessment Area Community Development Financing Metric (2.0 percent)

Banks with assets over $10 billion would be required to collect and maintain data about the geographic location of their deposits. Banks below this level would use FDIC Summary of Deposits data.

The CD Financing Metric as calculated above would be compared to one local and one national benchmark for each facility-based assessment area. The local benchmark, the Assessment Area Community Development Financing Benchmark, would be calculated by dividing the dollar amount of all large banks' CD loans and investments in the assessment area by the deposits they collect from the area, as illustrated below:

$$\text{Assessment Area Community Development Financing Benchmark} = \frac{\text{Annual average of local CD loans+CD investments}}{\text{Annual average of local deposits}}$$

The national benchmarks, the Metropolitan and Nonmetropolitan Nationwide Community Development Financing Benchmarks, would also be calculated by comparing all CD loans and investments made nationwide to deposits taken in metropolitan and nonmetropolitan areas, respectively.

$$\text{Nationwide Community Development Financing Benchmark-Metropolitan} =$$

$$\frac{\text{Annual average of nationwide metropolitan CD loans+CD investments}}{\text{Annual average of national metropolitan deposits}}$$

$$\text{Nationwide Community Development Financing Benchmark-Nonmetropolitan} =$$

$$\frac{\text{Annual average of nationwide nonmetropolitan CD loans+CD investments}}{\text{Annual average of national nonmetropolitan deposits}}$$

A conclusion in the Community Development Financing Test in a facility-based assessment would be based on consideration of the bank assessment area community development financing metric relative to the local and nationwide benchmarks, in conjunction with the previously described impact review of the bank's activities. This conclusion would be based on examiner judgment and would use the standard ratings of "Outstanding," "High Satisfactory," "Low Satisfactory," "Needs to Improve," or "Substantial Noncompliance." As data is collected, the agencies may eventually convert the CD Financing Test to being completely quantitative—rather than based on examiner judgement—but they said they lack the data to do so at this time.

Additional tests, using similar methodology, would be applied to bank lending conducted outside of a bank's assessment areas at both the state and whole institution level.

Large Banks: Community Development Services Test

The new CD Services Test would assess a large bank's record of helping to meet the community development services needs in the bank's facility-based assessment areas, states, multistate MSAs, and nationwide areas. The test would qualitatively consider the extent to which a bank provides community development services and the impact and responsiveness of these activities. Examiners could consider the following factors:

(i) The total number of community development service hours.
(ii) The number and type of community development service activities.
(iii) For nonmetropolitan areas, the number of activities related to the provision of financial services.

(iv) The number and proportion of community development service hours completed by, respectively, executive and other employees of the bank.
(v) The number of low- or moderate-income participants, organizations served, and sessions sponsored.
(vi) Other evidence that the bank's community development services benefit low- or moderate-income individuals or are otherwise responsive to a community development need.

For large banks with average assets of over $10 billion, the CD Services Test would include an additional quantitative benchmark to evaluate community development service hours. The metric would calculate the average number of community development service hours per full-time equivalent employee by dividing the hours of community development services activity in each facility-based assessment area during the evaluation period by the total full-time-equivalent employees in the facility-based assessment area. At first, this metric would not be compared to a specific benchmark to generate a presumptive conclusion, but a benchmark could be developed in coming years as data is collected.

Calculating Ratings

Large Banks — For large banks, the agencies propose to determine a bank's state, multistate MSA, and institution rating by combining the bank's performance scores across all four performance tests for the state, multistate MSA, or institution overall.

- The Retail Lending Test would be given a weight of **45 percent**.
- The Community Development Financing Test a weight of **30 percent**.
- The Retail Service and Products Test a weight of **15 percent**.
- The Community Development Services Test a weight of **10 percent**.

ISBs — For intermediate small banks, the agencies propose to weight the Retail Lending Test at 50 percent and the intermediate bank community development evaluation (or if the bank opts in, for the Community Development Financing Test) at 50 percent.

Small Banks — Small banks are only evaluated on the basis of retail lending, so the status quo small bank lending test, or the new Retail Lending Test if they opt in, would continue to account for 100 percent of their rating.

Transition

The rule would become effective **60 days** after publication of a final rule in the Federal Register. Publication of a final rule would likely happen several months after the end of the comment period in August. The following substantive provisions of the rule would take effect on the effective date and would likely require bank action within 60 days of a final rule:

(i) Facility-based assessment area delineation provisions.
(ii) Content and availability of public file.

For other provisions, the agencies propose an applicability date of approximately **12 months** after publication of a final rule. These provisions include:

(i) Definitions (except for the revised definitions related to small business loans and small farms loans).
(ii) Community development definitions.
(iii) Qualifying activities confirmation and illustrative list of activities.
(iv) Retail lending assessment areas.
(v) Areas for eligible community development activity.
(vi) Performance tests, standards, and ratings, in general (Retail Lending Test, Retail Services and Products Test, Community Development Financing Test, Community Development Services Test, Community Development Financing Test for Wholesale and Limited Purpose Banks, and Strategic Plans).
(vii) Data collection and certain data reporting requirements.
(viii) Impact Review of Community Development Activities.

Most of these changes are substantial and will require significant action by banks, particularly those subject to the large bank test.