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CRA Notes from the Field

Guidance for Maximizing Your Bank's Documentation

OVER THE LAST DECADE, I've had the amazing opportunity to chat with hundreds of bankers about their CRA programs and examination experiences. I've also worked closely with many CRA Officers as they utilized our software and consulting services to research and prepare for CRA exams. Through these relationships, I've learned many lessons about ongoing expectations for CRA documentation. While the CRA regulation and its interpretive guidance provide a guideline for banks to follow, in practice, documentation standards undergo adjustments in response to continuous changes in CRA examination teams, and as community needs evolve. Following are my notes from the field to consider when evaluating their CRA activities:

1 Documenting affordable housing isn't as simple as it seems.

When it comes to affordable housing, it may seem obvious when a loan or investment addresses this ever-increasing critical need in our communities. However, it's not that simple. Bank activities that support affordable housing can take on many different forms and structures, and with each change, the need for documenting their CRA qualification grows.

As outlined in the CRA regulation, affordable housing activities must serve low- or moderate-income (LMI) individuals, whether through the provision of single family or multifamily housing. In many cases, banks extend credit or invest in properties that are being constructed or rehabilitated using federal funding programs through agencies like the U.S. Department of Housing and Urban Development (HUD) or via specialized programs like the Low-Income Housing Tax Credit initiative. These funding programs are designed to ensure an affordable housing purpose.

However, there are thousands of other housing developments in cities across the nation that are not tied to these

government-backed funding sources. Especially in the case of multifamily housing, banks have an opportunity to earn additional CRA consideration. In the case of "naturally occurring affordable housing"—affordable housing developed without a government-backed program or funding—banks should investigate the intent and purpose of the housing developer and the targeted residents for the housing. Banks must be able to clearly evidence that the primary purpose of the housing meets CRA guidelines.

For many years, banks have compared the actual or proposed rents for new or existing housing developments to the national HUD Fair Market Rents published each year. When the rents related to a subject property being evaluated for CRA are at or below the HUD Fair Market Rents for the community where it is located, many banks have considered these properties as offering naturally occurring affordable housing. However, in recent months, I've heard from many bankers that this simple evaluation may not be enough.

It's also important to consider the intent of bank's borrower. Is the borrower actually intending to construct, pre-

serve, or rehabilitate the housing so that it will be affordable for LMI individuals? Alternatively, has the borrower told the bank that they intend to increase rents on vacant units or rehabbed units? Is the borrower simply buying another property to add to their investment portfolio and is indifferent to the affordable housing nature of the property itself?

Banks can also look to other factors related to the property and its residents to further support CRA characteristics. If the property is located in a LMI census tract or other geography with a documented affordable housing need, it can bolster the fact that the bank's loan is responsive to community needs. The bank could also evaluate the maximum affordable rents for a LMI individual based on the FFIEC's Median Family Income or the Area Median Income and compare that to the actual rents being offered at the subject property. Generally, an affordable rent should not exceed 30 percent of an individual's monthly gross income to be considered affordable. In the case of existing properties with current tenants, I've increasingly heard of banks being asked to provide documentation on the actual incomes of the current tenants to support that the tenants are LMI individuals.

In the case of Mortgage-Backed Securities, banks should request and maintain sufficient documentation to support that the Mortgage-Backed Securities are comprised of mortgage loans to LMI borrowers and what percentage of the properties are located within the bank's CRA Assessment Areas. For a large affordable housing fund or loan pool, banks may be asked to produce evidence as to how the bank's investment is responding to community needs.

2 Economic development activities have a two-prong test and are narrowly defined.

Within the four pillars of CRA, the economic development test is the only pillar that has its own detailed additional two-prong test for CRA qualification. For activities to receive credit under this area, they must pass both a size test and a purpose test. The purpose test includes activities such as the creation or retention of permanent jobs for LMI people or in LMI areas, including workforce development and job skills training, or the provision of technical assistance to small businesses and small farms such as shared space, technology, or administrative assistance. Documenting these aspects of a loan or investment can be pretty straight forward, but many banks overlook the size test in their consideration of economic development activities.

The size test stipulates that the bank's activity not only has to have a primary purpose of economic development, but that it also must be provided a business or farm that has gross annual revenues of \$1 million or less. Alternatively, the CRA regulation allows banks to consider size eligibility standards under the Small Business Administration's (SBA) Development Company or Small Business Investment Company programs to evidence that a business is a small business. The easiest option for a banker might be to evaluate the gross annual revenues of the business and if those revenues are over \$1 million, to assume that the loan does not meet the size test. However, the bank shouldn't necessarily stop there, as the alternative standards provide for greater flexibility. In some cases, this alternative regulatory approach to determining the classification of a small business diverges significantly from the conventional method of relying solely on revenues, instead opting to consider the number of employees as the primary metric for specific business types. Moreover, it introduces the possibility of raising the maximum threshold for gross annual revenues, surpassing the conventional \$1 million limit for select industries.

When evaluating incomes under the purpose test, a bank can ask a business directly for payroll data or projected incomes for new businesses to evidence that the majority of jobs being created are for LMI individuals. Banks also have the option to utilize data that is available on the Bureau of Labor Statistics' website to seek out average hourly and annualized wages for hundreds of industries and positions across each MSA and state in the nation.

Another common question I've been asked



is about chambers of commerce. In most cases chambers have a stated mission of providing "economic development" activities; however, it is critical that the bank does not simply rely on this mission statement to evidence that its activities with a chamber will receive CRA consideration. The bank must seek out and provide additional details as to how a specific chamber is aligned with the CRA purposes of economic development. Does it provide specialized programs and technical assistance to small businesses and small farms? Does it help to retain, improve, or create permanent jobs for LMI workers and geographies? If so, how? A tangential benefit will likely not be enough to receive credit for activities undertaken with these organizations without sufficient documentation to support their CRA primary purpose.

3 While all community service is good, it's not all equal under CRA.

Banks provide hundreds of donations, and service hours to nonprofits in their efforts to reinvest in the community. Documenting that fact for each organization and activity can be time-consuming, but I continue to hear from bankers about challenges to activities that haven't been sufficiently documented and ultimately disqualified during CRA examinations.

In the case of donations and employee service, bankers must clearly support how the organization, program, or population being served meets CRA requirements. While the CRA regulation itself provides the framework for evaluating these activities, the Interagency Questions & Answers on CRA ("Q&As"), last updated in 2016, provide a much deeper assessment and tools for banks to consider when researching qualification.

While a bank may know its communities, anecdotal information will not pass the test for CRA documentation. When accumulating information, the bank should gather details about how each organization or the program being supported meets the primary purpose of providing either affordable housing, economic development, etc. In the case of community services to LMI individuals, the bank should seek out a target letter or email or similar statement from the organization's representative as to the percentage of individuals served by the organization who qualify as LMI.

Unfortunately, for most nonprofits, income information regarding the individuals it serves may not exactly align with the CRA's definition of "low- or moderate-income." In many cases, nonprofits may not even ask for documentation of income from their clients. The good news is that the Q&As provide alternatives that banks can consider when documenting income that may be more readily available for nonprofits such as individuals who are eligible for Medicaid, HUD assistance, or the U.S. Department of Agriculture's (USDA's) Supplemental Nutrition Assistance program. The Q&As also extend this alternative to "any government assistance programs that have income qualifications equivalent to, or stricter than, the definitions of low- and moderate-income as defined by the CRA regulations."

In the case of donations or service provided to schools, with the 2016 update to the Q&As, the standard for evidencing CRA eligibility has been tied to schools where the majority of students qualify for free and reduced-price meals under the USDA's National School Lunch Program. Fortunately, banks can easily research the number of students in each public school across the nation that meet this requirement by visiting the National Center for Education Statistics' website.

4 Just because an activity is in a low- or moderate-income area doesn't mean it revitalizes or stabilizes the area.

As with other CRA activities, revitalization and stabilization activities must be responsive to community needs. Not every activity that occurs in a LMI census tract or a nonmetropolitan distressed or underserved census tract is automatically considered revitalizing or stabilizing. Such activities should attract or retain residents and businesses and should be undertaken in response to a government plan. In distressed or underserved areas, they can further support essential community facilities or infrastructure.

Identifying government plans can be an arduous task, as they are issued by state, local and Tribal governments as needed, and no centralized database exists for research. Also, not every government plan is designed to revitalize or stabilize a community in a way that corresponds to CRA. When researching government plans, banks must take the time to evaluate the scope and goals of the plans closely to ensure that a supported CRA primary purpose can be documented. It's also imperative that the bank evaluate the geographic focus of the plan to ensure that the targeted geography of the bank's activity is within the covered plan area.

In regard to disaster recovery, again, not every activity that a bank undertakes in a disaster area will be automatically considered for CRA. Under the Q&As, activities need to be responsive to the disaster relief, excluding debris removal and public emergency measures. The area must also be designated by the government as disaster area, evidenced by a FEMA major disaster declaration.

5 Performance context is increasing in importance.

Gathering documentation is important, but the bank's individual listing of qualified activities may not be enough to ensure a satisfactory CRA rating. Increasingly, banks are being asked for detailed performance context information to explain community needs and how the bank has responded to those needs through its CRA activities.

While bankers may be familiar with the economic and demographic summaries provided in their CRA Public Evaluation reports, bankers should embrace and dedicate time to building a strong performance context written narrative that dives deep into a variety of areas. Not only should the bank understand the external

economic and demographic factors affecting its communities but should also interpret how those externalities impact the bank's lending, investment, and service opportunities and actual results during the examination cycle.

Explaining in detail how the bank's activities are meeting community needs can make the difference between an activity receiving CRA credit and not during your next examination. Spend time talking with community leaders and the organizations you support to highlight how the bank's involvement made a difference to their clients and the community they serve. Be sure to write it down and include it as part of your documentation.

It's also important to know what other banks in your Assessment Areas are doing. It's one thing to have a general understanding of who your competitors are, but to truly understand your CRA opportunities and risks, a bank must conduct a detailed analysis of similarly situated banks and compare that to its own performance. While many banks evaluate aggregate and demographic comparators for lending performance, they often don't extend this comparative activity to their Community Development Loans, qualified investments, and service hours. This leaves a black hole in benchmarking and a critical risk in managing CRA expectations. Time spent identifying peers for community development activities and calculating related benchmarks based on that research will increase bank confidence and help with CRA goal setting. Unfortunately, the accumulation of data related to similarly situated banks when it comes to community development performance relies on a deep dive into the CRA Public Evaluation reports available online.

6 Ditch the scrapbook for strong, clear narratives and supporting documentation.

While scrapbooking is a fun hobby, it should not be a bank's approach to CRA documentation. During some CRA consulting engagements, I personally have been sent virtual files full of random newspaper clippings, lists, pictures, and website screen prints. While all of this information may tell a great story, during a limited examination timeframe, your bank examiner will not have time to piece the puzzle together and interpret the documents into a cohesive CRA narrative. Sadly, this often means a bank will lose credit for many CRA activities.

Organization in CRA documentation is key. While a bank may work on its CRA documen-

tation for years, there's only a short time frame to illustrate that impact during the examination. The less ambiguity in documentation, the better. Prior to the examination, ensure that you have identified all activities that you're submitting for credit and have gathered all of your supporting documentation in standardized, consistent formats. If you use an online tracking software, make sure the reports are formatted and ready before you need them. If you want your examiner to understand key aspects about your CRA activities, provide written narratives. Don't assume that the story you want to come through will be interpreted correctly—tell the story you want to tell.

By spending the time conducting the research, crafting your performance context, and organizing your CRA documentation, you can streamline the next examination experience and ensure your bank receives credit for all the important work you do. ■

ABOUT THE AUTHOR



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ABA MEMBER RESOURCES

ABA Advocacy: Community Reinvestment Act Modernization
[aba.com/advocacy/our-issues/community-reinvestment-act-modernization](https://www.aba.com/advocacy/our-issues/community-reinvestment-act-modernization)

ABA Webinar: Drive economic growth through your CRA program
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