

representing direct obligations of the SPV collateralized by its assets, or trust certificates or other beneficial interests in the SPV's assets ("SPV Obligations"). However, the SPV Obligations will not represent equity investments in the SPV itself.

The Intermediary will privately place SPV Obligations with financial institutions subject to the CRA. The proposal indicates that whether the SPV Obligations will take the form of loans to the SPV or the form of beneficial interests in the assets of the SPV has not been determined. Therefore, it is unclear whether financial institutions will account for their purchases of the SPV Obligations as securities or as loans.³ Depending on the form of the SPV Obligations, financial institution investors will be informed of their percentage financing of the SPV or their percentage beneficial interest in the assets of the SPV. The financial institutions will also be informed of the percentage of assets held by an SPV that are collateralized by affordable housing mortgages.

II. DISCUSSION

You requested an opinion (1) whether the purchase of SPV Obligations would receive favorable CRA consideration under the different evaluation methods contained in the amended CRA regulations (including the evaluation methods applicable to large retail institutions, wholesale or limited purpose institutions, small institutions and institutions evaluated on the basis of a strategic plan); (2) whether the CRA consideration would be affected if some of the mortgages held by an SPV were from middle- and upper-income individuals; (3) whether the CRA consideration would be affected if the mortgages held by an SPV were on properties located in a statewide or regional area that includes an institution's assessment area(s), but few or no mortgages were on properties located in the institution's assessment area(s); (4) what specific tests and performance standards would result in favorable CRA consideration; and (5) whether a financial institution that purchases an SPV Security prior to July 1, 1997 would receive positive consideration (a) if it is examined prior to July 1, 1997 and (b) if it is examined subsequent to July 1, 1997.⁴

Depending on the form and booking of the obligations, the purchase of obligations like the SPV Obligations would warrant favorable CRA consideration under the investment test, lending test (as a loan to the SPV, but not as loans to the home buyers) or the community development test (as a qualified investment in or loan to the SPV, but not as loans to the home

³ How the SPV Obligations will be carried on an institution's books must be determined consistent with safety and soundness, as well as any other applicable laws, regulations, and guidelines.

⁴ This letter addresses only these five issues. It does not address whether a purchase of SPV Obligations would be lawful. Federal law limits the types of investment securities that financial institutions may purchase for their own account. *See, e.g.*, 12 U.S.C. §§ 24(Seventh) & (Eleventh) (applicable to national banks), 335 (state member banks), 1831a(c) and (f) (state non-member banks), and 1464(c) (federal thrifts). The CRA does not provide financial institutions with any independent authority to make loans or investments. Furthermore, the agencies do not endorse particular lending or investment products.

buyers). In addition, as a lending-related investment, the purchase of obligations like the SPV Obligations would be considered a “lending-related activity,” which would be considered under small institution performance standards.⁵ Finally, the purchase of obligations like the SPV Obligations may also be considered in connection with an institution’s strategic plan.

A. Definition of Qualified Investment; the Effect of Including Mortgages from Middle- and Upper-Income Individuals and Families

Because it has not yet been determined whether the SPV Obligations will take the form of loans to the SPV or the form of beneficial interests in the assets of the SPV, this section discusses the purchase of SPV Obligations that are carried on the institution’s books as investment securities, rather than as loans.

The revised CRA regulations define a “qualified investment” as “a lawful investment, deposit, membership share or grant that has as its primary purpose community development.”⁶ “Community development” means, *inter alia*, “affordable housing (including multifamily rental housing) for low- or moderate-income individuals.”⁷ “Low-income” is defined as less than 50 percent of area median income, and “moderate-income” is defined as at least 50 percent and less than 80 percent of area median income.⁸

An institution’s purchase of obligations like SPV Obligations would be considered a qualified investment if the assets of the SPV consist of mortgages *primarily* from individuals and families earning below 80 percent of the area median income and the SPV Obligations are carried as investment securities on the institution’s books. The fact that some of the mortgages held by an SPV may be from individuals and families earning at or above 80 percent of the area median income (i.e., middle- and upper-income) would not, of itself, disqualify the purchase of SPV Obligations as a qualified investment.

B. Geographic Benefit Requirement

⁵ See Community Reinvestment Act; Interagency Questions and Answers Regarding Community Reinvestment, 61 Fed. Reg. 54,647, 54,658-59 (Oct. 21, 1996) (questions and answers 1 and 5 addressing § __.26(a)).

⁶ 12 C.F.R. §§ 25.12(s), 228.12(s), 345.12(s), and 563e.12(r).

⁷ 12 C.F.R. §§ 25.12(h)(1), 228.12(h)(1), 345.12(h)(1), and 563e.12(g)(1).

⁸ 12 C.F.R. §§ 25.12(n)(1) and (2), 228.12(n)(1) and (2), 345.12(n)(1) and (2), and 563e.12(m)(1) and (2). Your letter implies that the upper limit of “moderate-income” is 80 percent of area median income. Please note that, for purposes of the CRA regulations, the upper limit of “moderate-income” is *less* than 80 percent of area median income.

Under the revised CRA regulations, qualified investments generally must benefit the institution's assessment area(s) or a broader statewide or regional area that includes the institution's assessment area(s) in order to receive favorable CRA consideration. This geographic benefit requirement is applicable to the purchase of SPV Obligations by an institution evaluated under the investment test.⁹ The community development test for wholesale and limited purpose institutions also requires that the purchase of SPV Obligations benefit the institution's assessment area(s) or a broader statewide or regional area that includes the institution's assessment area(s), unless the institution has otherwise adequately addressed the needs of its assessment area(s).¹⁰ Although not explicit in the regulation, the agencies' staff also believe that the purchase of SPV Obligations by a small institution should benefit the institution's assessment area(s) or a statewide or regional area that includes the institution's assessment area(s) in order to receive favorable CRA consideration.¹¹ Whether the purchase of SPV Obligations by an institution that is evaluated on the basis of a strategic plan must benefit the institution's assessment area(s) or a broader statewide or regional area that includes the institution's assessment area(s) depends on the institution's goals as stated in the strategic plan.¹²

The agencies recently published "Questions and Answers Regarding Community Reinvestment" to provide guidance about the CRA regulations.¹³ Two questions and answers (Qs and As) provide helpful information regarding your inquiry about geographic benefit. First, Q and A 5, which addresses § __.12(i) & 563e.12(h),¹⁴ states that there need not be an

⁹ 12 C.F.R. §§ 25.23(a), 228.23(a), 345.23(a), 563e.23(a).

¹⁰ 12 C.F.R. 25.25(e)(1), 228.25(e)(1), 345.25(e)(1) and 563e.25(e)(1). Wholesale and limited purpose institutions can receive favorable CRA consideration for qualified investments regardless of the benefit to their assessment area(s) (or the broader statewide or regional area that includes the assessment area(s)) if they have adequately addressed community development needs in their assessment area(s). 12 C.F.R. §§ 25.25(e)(2), 228.25(e)(2), 345.25(e)(2), and 563e.25(e)(2).

¹¹ Examiners may adjust their assessment of a small institution's loan-to-deposit ratio based on the institution's holdings of qualified investments. 12 C.F.R. §§ 25.26(a)(1), 228.26(a)(1), 345.26(a)(1), and 563e.26(a)(1). For example, the examiner may conclude that an otherwise low loan-to-deposit ratio is counter-balanced by the fact that a small institution has a significant amount of qualified investments. Qualified investments may also be considered to determine if a small institution merits an "outstanding" CRA rating. 12 C.F.R. pt. 25 app. A(d)(2), pt. 228 app. A(d)(2), pt. 345 app. A(d)(2) and pt. 563e app. A(d)(2). *See also* Community Reinvestment Act; Interagency Questions and Answers Regarding Community Reinvestment, 61 Fed. Reg. 54,647, 54,658 (Oct. 21, 1996) (questions and answers 1 and 5 addressing § __.26(a)).

¹² Institutions evaluated on the basis of a strategic plan must include in their plan measurable goals for helping to meet credit needs of their assessment area(s) through lending, *investment*, and/or services, as appropriate. 12 C.F.R. §§ 25.27(f)(1), 228.27(f)(1), 345.27(f)(1), and 563e.27(f)(1) (emphasis added).

¹³ *See* 61 Fed. Reg. 54,647 (Oct. 21, 1996).

¹⁴ 61 Fed. Reg. at 54,651.

immediate or direct benefit to an institution's assessment area(s) to satisfy the regulations' requirement that qualified investments (and community development loans) benefit an institution's assessment area(s) or a broader statewide or regional area that includes the institution's assessment area(s). An institution's investment or activity is considered a qualified investment or community development loan if it supports an organization or activity that covers an area that is larger than, but includes, the institution's assessment area(s). The institution's assessment area need not receive an immediate or direct benefit from the institution's specific participation in the broader organization or activity, provided the purpose, mandate, or function of the organization or activity includes serving geographies or individuals located within the institution's assessment area(s).

Q and A 6, which also addresses § __.12(i) & 563e.12(h),¹⁵ discusses what is meant by a "regional area." It explains that a regional area may be as small as a city or county or as large as a multistate area. It also cautions that when examiners evaluate community development loans (or qualified investments) that benefit a regional area that includes the institution's assessment area(s), they will consider the size of the regional area and the actual or potential benefit to the institution's assessment area(s). In most cases, the larger the regional area, the more diffuse the benefit will be to the institution's assessment area(s). Examiners may view loans (or qualified investments) with more direct benefits to an institution's assessment area(s) as more responsive to the credit needs of the area(s) than loans (or investments) for which the actual benefit to the assessment area(s) is uncertain or for which the benefit is diffused throughout a larger area that includes the assessment area(s).

C. CRA Consideration of SPV Obligations Booked as Loans

This section discusses the purchase of SPV Obligations that are carried on institution's books as loans. Community development loans purchased by an SPV would not be attributed to institutions that purchase SPV Obligations. However, the institutions could receive favorable CRA consideration for making a community development loan to the SPV, through the purchase of SPV Obligations.

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.¹⁶ Like a qualified investment, a "community development loan" must have community development as its primary purpose and must benefit the institution's assessment area(s) or a broader statewide or regional area that includes the institution's assessment

¹⁵ *Id.*

¹⁶ 12 C.F.R. §§ 25.22(b)(4), 228.22(b)(4), 345.22(b)(4), and 563e.22(b)(4).

area(s).¹⁷ The considerations regarding whether the purchase of SPV Obligations would be considered to have community development as its primary purpose, and whether the geographical benefit requirement would be satisfied, are the same as those discussed above, with respect to the definition of “qualified investment.”

Assuming that the purchase of a security like SPV Obligations would be considered to have community development as its primary purpose, that the purchase would benefit the institution’s assessment area or a broader statewide or regional area that includes the institution’s assessment area, and that the transaction is booked as a loan on the institution’s books, the purchase of the security would qualify as a community development loan to the SPV, provided it is not required to be reported as a small business loan.¹⁸

However, when conducting a CRA examination, examiners will not consider a share of the underlying loans purchased by an SPV to be attributable to the purchaser of SPV Obligations. Under the lending test, community development loans originated by a third party in which an institution has invested will be considered, at the institution’s option, subject to certain limitations.¹⁹ The agencies consider an institution to have “invested” in a third party within the meaning of this provision when the institution has made an equity, or equity-like, investment in the third party -- not when the institution has made a loan to, or purchased an ordinary debt obligation of, the third party.²⁰

Under the proposal you submitted, the institutions will purchase SPV Obligations that represent a percentage investment in the assets of the SPV. The proposed structure does not provide institutions with an equity or equity-like investment in the SPV itself. Therefore, a pro rata share of the community development loans purchased by the SPV would not be attributed to financial institution investors that purchase SPV Obligations under the lending test. Thus, under the lending test, an institution that purchases SPV Obligations could receive favorable CRA consideration for making a community development loan to the SPV (if the SPV Obligations are accounted for by the institution as loans rather than investments), but the

¹⁷ 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). A wholesale or limited purpose institution can also receive consideration for qualified investments that benefit areas outside the institution’s assessment area(s) (or a broader statewide or regional area that includes the institution’s assessment area(s)) if the institution has adequately addressed the needs of its assessment area(s). 12 C.F.R. §§ 25.25(e), 228.25(e), 345.25(e), and 563e.25(e).

¹⁸ Loans that have been reported as small business loans may not also be considered as community development loans (except in the case of wholesale and limited purpose institutions). *See* 12 C.F.R. §§ 25.12(i)(2)(i), 228.12(i)(2)(i), 345.12(i)(2)(i), and 563e.12(h)(2)(i). *See also* Q and A 2 addressing § __.42(b)(2), 61 Fed. Reg. at 54,665.

¹⁹ 12 C.F.R. §§ 25.22(d), 228.22(d), 345.22(d), and 563e.22(d).

²⁰ *See* Q and A 1 addressing § __.22(d), 61 Fed. Reg. at 54,657.

underlying loans purchased by the SPV would not be attributable to the institution.

D. Transition Period

On July 1, 1997, the amended CRA regulations will apply to all institutions.²¹ Therefore, an institution that purchases SPV Obligations prior to July 1, 1997 and is examined after July 1, 1997 would be evaluated as described above.

The amended CRA regulations became effective for small institutions on January 1, 1996. Also, any institution may elect to be evaluated under the amended CRA regulations as of January 1, 1996. Therefore, small institutions and institutions that elect to be evaluated under the amended regulations also would be evaluated as described above.

However, an institution that purchases SPV Obligations prior to July 1, 1997, is examined prior to July 1, 1997, is not a small institution, and does not elect to be evaluated under the amended CRA regulations would be evaluated under the previous CRA regulations.

The previous CRA regulations list twelve assessment factors used to evaluate CRA performance. At least two of those factors could provide a basis for favorable CRA consideration of an institution's purchase of SPV Obligations. The eighth assessment factor provides that the agencies will consider an institution's "participation, including investments, in local community development and redevelopment projects or programs."²² The twelfth assessment factor allows the agencies to consider other factors that reasonably bear upon the extent to which an institution is helping to meet the credit needs of its entire community.²³

When compared to the amended CRA regulations, the previous regulations' geographic focus is more narrow, largely limited to an institution's delineated community. Nevertheless, under the previous CRA regulations, the agencies recognized that institutions may use a wide variety of programs, organizational mechanisms or intermediaries to help finance low- and moderate-income housing on a statewide or regional basis. The agencies also recognized that although some of these activities may benefit an institution's delineated community, they often provide the bulk of their benefits to other geographical areas. The agencies provided the following guidance under the previous CRA regulations, which continues to be applicable to evaluations under those regulations:

Under certain circumstances, the agencies will give positive consideration in

²¹ 12 C.F.R. §§ 25.51, 228.51, 345.21 and 563e.21.

²² 12 C.F.R. §§ 25.7(h), 228.7(h), 345.7(h) and 563e.7(h).

²³ 12 C.F.R. §§ 25.7(l), 228.7(l), 345.7(l) and 563e.7(l).

assessing CRA performance for active participation by a financial institution in such programs and mechanisms, even where most or all of the financing provided may ultimately benefit low- and moderate-income borrowers or neighborhoods located outside of the institution's delineated community. In determining whether and to what extent positive consideration will be given, the agencies assess the activities undertaken in the context of the institution's overall CRA program. Where such participation augments or complements an overall CRA program that is directly responsive to the credit needs in an institution's delineated community, it will be considered favorably in reaching an overall CRA conclusion. However, such activities and involvements will be insufficient to compensate for an otherwise deficient record of addressing the credit needs of a institution's delineated community.²⁴

Thus, under the previous CRA regulations, an institution that has adequately addressed the credit needs of its delineated community would receive favorable CRA consideration for the purchase of SPV Obligations regardless of the location of the loans backing the securities. Otherwise, favorable CRA consideration generally would be limited to the benefits accruing to the institution's delineated community from the SPV's activities.

III. CONCLUSION

I trust that this letter has been responsive to your inquiry. If you have any further questions, please feel free to contact me or Margaret Hesse of my staff at (202) 874-5750.

Sincerely,

\s\

Michael Bylsma
Acting Director
Community and Consumer Law Division
Office of the Comptroller of the Currency

²⁴ 58 Fed. Reg. 9,176, 9,180 (Feb. 19, 1993).