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

**Interpretive Letter #792
August 1997
12 U.S.C. 2901**

July 25, 1997

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Dear []:

This letter responds to your April 24, 1997 letter requesting an opinion about the applicability of the Community Reinvestment Act ("CRA") to financial institutions' investments in the [] (the "Fund"). As you know, the four federal bank and thrift regulatory agencies ("Agencies") promulgated substantially similar CRA regulations on May 4, 1995. In order to promote consistent interpretation of these CRA regulations, staff from all four agencies have considered your inquiry and concur in the opinions expressed in this letter.

I. Background

In your letter, you explain that the Fund was established as a vehicle for investors to invest in women-owned businesses located in the Mid-Atlantic region. Investors can purchase a limited partnership interest in the Fund for \$100,000. These investments will be used by the Fund to invest in approximately 15 women-owned businesses. Some of these businesses will meet the size eligibility standards of the Small Business Administration's Development Company or Small Business Investment Company programs (13 CFR 121.301) or have gross annual revenues of \$1,000,000 or less.

Your letter further explains that financial institutions will invest in the Fund through their bank holding companies. These companies will designate a specific geographic area in which the Fund will invest a portion of its assets. The Fund will inform the holding company of the amount it has invested in the targeted geographic area. Where more than one holding company has designated the same area, the Fund will allocate between the companies the

amount it has invested in that area.

II. Discussion

In your letter, you ask whether a financial institution that invests in the Fund would “receive positive consideration under the CRA regulations for its entire investment in the Fund to the extent the Fund makes qualified investments in the banking institution’s assessment area(s), with proportional consideration being given where the Fund has invested in companies located in an assessment area designated by more than one banking institution.”¹ This question raises three issues: (A) May an institution that invests in an entity, such as the Fund, that supports small businesses in the institution’s assessment area receive positive consideration for making a “qualified investment” under the CRA regulations?; (B) Would the institution receive positive consideration only for such investments and only to the extent that they provide direct benefits to the institution’s assessment area?; and (C) How much consideration will examiners give to an institution’s investment in an entity, such as the Fund, where another institution has also invested in the fund and designated the same assessment area in which the entity will support small businesses? These issues are addressed below.

A. Qualified Investments in Small Businesses

The CRA regulations establish the framework and criteria by which the Agencies assess an institution’s record of helping to meet the credit needs of its community. The CRA regulations set out a number of different evaluation methods for examiners to use, depending on the business strategy and size of the institution under examination.

Regardless of the performance test under which a regulated financial institution is evaluated,²

¹ Your letter also indicates that a portion of the Fund’s offering memorandum will describe this interpretive letter. Please note that this letter addresses only whether an investment in an entity that supports small businesses would receive favorable CRA consideration. It does not address whether such an investment would be lawful. 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.

² Large institutions’ CRA performance is typically evaluated under the lending, investment and service tests. Examiners consider large institutions’ qualified investments under the investment test. See 12 C.F.R. §§ 25.23(a), 228.23(a), 345.23(a), and 563e.23(a). In a small institution examination, examiners may adjust an institution’s evaluation under the small institution performance criteria, if appropriate, based on lending-related qualified investments. See 12 C.F.R. §§ 25.26(a)(1), 228.26(a)(1), 345.26(a)(1), and 563e.26(a)(1). See also Community Reinvestment Act; Interagency Questions and Answers Regarding Community Reinvestment (hereinafter “Qs and As”), 61 Fed. Reg. 54,647, 54,658 (Oct. 21, 1996) (Q and A 1 addressing § __.26(a) (consideration of small institutions’ lending-related activities)). Qualified investments may also be considered to determine if a small institution merits an outstanding CRA rating. See 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 Q and A 5 addressing § __.26(a), 61 Fed. Reg. at 54,659. The community development test, which is appropriate for wholesale and limited purpose institutions, evaluates, *inter alia*, the number and amount of qualified investments. See 12 C.F.R. §§ 25.25(c)(1), 228.25(c)(1), 345.25(c)(1),

an institution can receive positive consideration for making “qualified investments” that help meet the credit needs of the institution’s assessment area(s) or a broader statewide or regional area that includes the institution’s assessment area(s).³

“Qualified investment” is defined in the revised CRA regulations as:

[A] lawful investment, deposit, membership share or grant that has as its primary purpose community development.⁴

“Community development” is defined to include:

Activities that promote economic development by financing businesses or farms that meet the size eligibility standards of the Small Business Administration’s Development Company or Small Business Investment Company programs (13 CFR 121.301) or have gross annual revenues of \$1 million or less.⁵

Financing businesses meeting the above size eligibility standards does not always necessarily promote economic development. The Agencies’ examiners will presume that any loan to or investment in a Small Business Development Company or Small Business Investment Company promotes economic development. Other activities that finance small businesses that meet the size eligibility standards must support permanent job creation, retention, and/or improvement for persons who are currently low- or moderate-income or support permanent job creation, retention, and/or improvement in low- or moderate-income geographies targeted for redevelopment by Federal, state, local or tribal governments.

A financial institution’s investment in an entity such as the Fund may have as its primary purpose community development. The Fund will provide financing for small businesses in the

and 563e.25(c)(1). And, finally, institutions evaluated on the basis of a strategic plan must include in their plan how they intend to meet the credit needs of their assessment area(s). They may meet credit needs through lending, *investment*, and/or services, as appropriate. See 12 C.F.R. §§ 25.27(f)(1), 228.27(f)(1), 345.27(f)(1), and 563e.27(f)(1) (emphasis added).

³ See 12 C.F.R. §§ 25.23(a), 25.25(e)(1), 25.26(a), 25.27(f)(1)(i), 228.23(a), 228.25(e)(1), 228.26(a), 228.27(f)(1)(i), 345.23(a), 345.25(e)(1), 345.26(a), 345.27(f)(1)(i), 563e.23(a), 563e.25(e)(1), 563e.26(a), and 563e.27(f)(1)(i). See also Q and A 2 addressing § __.26(b), 61 Fed. Reg. at 54,659-60 (consideration of a small institution’s qualified investments in a statewide or regional area that includes the institution’s assessment area(s)). In the case of wholesale and limited purpose institutions, examiners will give positive consideration to qualified investments nationwide if the institution has adequately addressed the needs of its assessment area(s). See 12 C.F.R. §§ 25.25(e)(2), 228.25(e)(2), 345.25(e)(2), 563e.25(e)(2).

⁴ 12 C.F.R. §§ 25.12(s), 228.12(s), 345.12(s) and 563e.12(r). This letter assumes, without deciding, that the financial institutions’ contributions to the Program would be lawful.

⁵ 12 C.F.R. §§ 25.12(h)(3), 228.12(h)(3), 345.12(h)(3), and 563e.12(g)(3).

Mid-Atlantic area that may meet the size eligibility standards discussed above and the financing of which may promote economic development. An institution may receive positive consideration for its investment in an entity, such as the Fund, provided that the investment helps meet the credit needs of the institution's assessment area(s), or a broader statewide or regional area that includes the institution's assessment area(s), by supporting small businesses meeting those size eligibility standards and financing them will promote economic development.⁶

B. Qualified Investments that Benefit Areas Outside of an Institution's Assessment Area(s)

An institution may receive positive consideration for its entire investment in an entity, such as the Fund, even if the investment is not used by the entity to make qualified investments exclusively in that institution's assessment area. As explained above, an institution may receive positive consideration for qualified investments that help meet the credit needs of the institution's assessment area(s) *or a broader statewide or regional area that includes the institution's assessment area(s)*. A regional area may be as small as a city or county or as large as a multistate area, such as the Mid-Atlantic region. See Community Reinvestment Act; Interagency Questions and Answers Regarding Community Reinvestment, 61 Fed. Reg. 54,647, 54,658 (Oct. 21, 1996) (Q and A 6 addressing § __.12(i) & 563e.12(h)).

The CRA regulations recognize that community development organizations and programs, which often operate on a statewide or multistate basis, can be effective ways for institutions to promote community development. As explained in the Interagency Questions and Answers Regarding Community Reinvestment, a qualified investment in such an organization or program need not provide an immediate or direct benefit to an institution's assessment area(s) in order to satisfy the requirement that a qualified investment benefit an institution's assessment area(s) or a broader statewide or regional area that includes the institution's assessment area(s):

[A]n institution's activity is considered a . . . qualified investment if it supports an organization or activity that covers an area that is larger than, but includes, the institution's assessment areas(s). The institution's assessment area need not receive an

⁶ A financial institution may receive positive consideration for such investments even if they are made by the institution's holding company rather than by the institution itself. At the financial institution's request, the institution's regulator will consider, "in its assessment of the [institution's] investment performance, a qualified investment made by an affiliate of the bank, if the qualified investment is not claimed by any other institution." See 12 C.F.R. §§ 25.23(c), 228.23(c), 345.23(c) and 563e.23(c). Thus, a bank holding company that invests in an entity such as the Fund may allocate to an affiliated financial institution the qualified investments made by the Fund as a result of that investment. That affiliated institution could then ask its regulator to consider those qualified investments during its CRA evaluation provided that no other institution requests consideration of the same qualified investments.

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.

See Community Reinvestment Act; Interagency Questions and Answers Regarding Community Reinvestment, 61 Fed. Reg. 54,647, 54,658 (Oct. 21, 1996) (Q and A 5 addressing § __.12(i) & 563e.12(h)).

C. Qualified Investments that Benefit Shared Assessment Area(s)

Your letter raises the question of what happens when more than one institution invests in the Fund and designates the same assessment area in which the Fund is to support small businesses. For example, two institutions invest \$100,000 each in the Fund and designate Eastern Maryland as the area in which the Fund should invest in small businesses. The Fund makes a \$100,000 qualified investment in a business located in Eastern Maryland and makes another \$100,000 qualified investment in a business located elsewhere in the Mid-Atlantic region. The Fund then reports to each institution that it has used \$50,000 of the institution's investment to support the Eastern Maryland business and the remaining \$50,000 to support other Mid-Atlantic businesses. How much consideration would the Agencies' examiners give to each institution's investment?

As explained above, the CRA regulations permit an institution to request consideration of qualified investments that benefit its assessment area(s) or a broader regional area that includes the assessment area(s). Thus, in the above example, both institutions would receive consideration of their respective total \$100,000 qualified investments as investments that benefit a broader regional area that includes their assessment area(s).⁷ However, in evaluating the qualified investment's responsiveness to the credit needs of the institutions' assessment area(s), examiners may, if circumstances warrant doing so, accord greater consideration to the portion of each institution's investment that directly benefited the area(s).⁸

III. Conclusion

Subject to the restrictions discussed above, an institution that invests in an entity such as the Fund may receive positive consideration in its CRA evaluations for the entire amount of its investment that results in qualified investments that benefit the institution's assessment area(s) or a broader area that includes its assessment area(s). Depending on the circumstances, however, examiners may accord greater weight to qualified investments that provide direct

⁷ See 12 CFR §§ 25.23(e)(1), 228.23(e)(1), 345.23(e)(1), and 563e.23(e)(1).

⁸ See 12 CFR §§ 25.23(e)(3), 228.23(e)(3), 345.23(e)(3), and 563e.23(e)(3).

benefits to the institution's assessment area(s). Where two institutions share the same assessment area invest in the entity, and the entity allocates the institutions' investments between that assessment area and a broader regional area that includes the institutions' assessment area, the investing institutions would receive positive consideration of their total investments in the entity.

I trust this letter is responsive to your inquiry. If you have further questions, please contact me or Michele Meyer, an attorney on my staff, at (202) 874-5750.

Sincerely,

/s/

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