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The Interagency Community Reinvestment Act Final Rule

By Randy Benjenk, Karen Solomon, Graves Lee and Emily Hooker*

In this article, the authors discuss the final rule from the federal banking agencies that overhauls the regulatory framework for evaluating banks' performance under the Community Reinvestment Act.

The Board of Governors of the Federal Reserve System, the Federal Deposit Insurance Corporation, and the Office of the Comptroller of the Currency (collectively, the agencies) have released a final rule[1] to overhaul the agencies' regulatory framework for evaluating banks' performance under the Community Reinvestment Act (CRA). The final rule concludes a rulemaking process stretching back more than five years, following a 2022 interagency notice of proposed rulemaking (the proposal)[2] and an earlier, abandoned effort by the OCC to make changes to its own CRA rule. The final rule makes the most significant interagency changes to the agencies' CRA regulations in more than 25 years, and will substantially alter CRA compliance obligations for banks of varying sizes and business models.

This article provides key takeaways for large banks, which the final rule defines as banks with $2 billion or more in assets.

MOST PROVISIONS OF THE FINAL RULE WILL BECOME OPERATIVE AT THE BEGINNING OF 2026

While the final rule becomes effective on April 1, 2024, a large bank will need to comply with most of the final rule's operative provisions – including assessment area requirements and performance tests – beginning January 1, 2026. Data reporting under the final rule will begin in early 2027. The proposal would have provided just a year for compliance with most of its key requirements, which prompted substantial pushback from commenters.

NEW GEOGRAPHIES WILL BE SUBJECT TO EVALUATION, CREATING CHALLENGES AND OPPORTUNITIES

Under the final rule, a large bank could be required to delineate two types of assessment areas in which its CRA evaluation will be focused:

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1 https://www.federalreserve.gov/aboutthefed/boardmeetings/frn-cra-20231024.pdf.

2 https://www.federalregister.gov/documents/2022/06/03/2022-10111/community-reinvestment-act.

- A bank must delineate "facility-based assessment areas" encompassing any Metropolitan Statistical Area, one or more contiguous counties within an MSA, or one or more contiguous counties within the nonmetropolitan area of a state in which the bank maintains a main office, branch, or other staffed or deposit-taking remote service facility, as well as surrounding geographies in which the bank has originated or purchased a substantial portion of loans. Facility-based assessment areas are generally the same as assessment areas under the existing CRA regulations, except that the minimum size of a facility-based assessment area has increased to be at the county level.
- Solely for purposes of the Retail Lending Test (described below), a bank may also be required to delineate "retail lending assessment areas" encompassing (1) any metropolitan statistical area, excluding counties already included within a facility-based assessment area, or an aggregation of all of the nonmetropolitan areas in a single state, excluding counties already in a facility-based assessment area or in which the bank did not originate any closed-end home mortgage loans or small business loans that year, in which (2) the bank originated at least 150 closed-end home mortgage loans or 400 small business loans for two consecutive calendar years. The final rule increased these loan origination thresholds from those contained in the proposal.

The final rule contains a key carve-out to the retail lending assessment area framework. A large bank that conducts 80 percent or more of specified retail lending activity (which for most banks will be home mortgage loans, small business loans, small farm loans, and multifamily loans) within its facility-based assessment areas over a two-year period is exempt from the requirement to delineate retail lending assessment areas the following year. This carve-out is likely to apply to large banks with robust branch networks.

The Retail Lending Test will also evaluate any large bank's retail lending distribution in an "outside retail lending area," meaning the residual nationwide area where the bank originated or purchased covered loans outside of its facility-based assessment areas and retail lending assessment areas. If a large bank originates or purchases even a single closed-end home mortgage, small business, or small farm loan (or automobile loan if majority automobile lender) in the outside retail lending area during the evaluation period, there is no carve-out to the outside retail lending area requirement.

While the new geographies subject to evaluation in the Retail Lending Test could create pitfalls for large banks, the final rule also creates greater opportunities for large banks to receive favorable consideration for community development activities conducted outside their facility-based assessment areas.

THE FINAL RULE LARGELY MAINTAINS THE PROPOSED LARGE BANK EVALUATION FRAMEWORK, WITH SOME SIMPLIFICATIONS AND TWEAKS

Like the proposal, the final rule sets forth four performance tests to which large banks will be subject. Each test contains a number of sub-tests, which could easily produce dozens of scores, conclusions, and ratings of different facets of a bank's performance across various geographies.

Test 1: Retail Lending Test

The Retail Lending Test evaluates whether the retail lending activities of the bank meet the needs of low- and moderate-income (LMI) individuals, small businesses, and small farms, and individuals and businesses in LMI census tracts. Under the final rule, the Retail Lending Test focuses on the distribution of a bank's closed-end home mortgage loans, small business loans, and small farm loans, as well as automobile loans if automobile lending makes up a majority of the bank's retail lending activity (or if the bank elects to have automobile lending included). This product focus departs from the proposal, which would have also included open-end home mortgage loans and multi-family loans, and would have included automobile loans for all banks.

The Retail Lending Test begins with a retail lending screen that assesses a bank's volume of retail lending (including originations and purchases) relative to its deposit base in each facility-based assessment area. If a bank's ratio falls below 30% of the market ratio, the bank is only eligible for a "Needs to Improve" or "Substantial Noncompliance" conclusion in the assessment area unless certain contextual factors explain the shortfall. The numerator of the retail lending screen includes open-end home mortgages and multifamily loans in addition to the products evaluated in the Retail Lending Test's distribution analysis (i.e., closed-end home mortgages and small business and small farm loans for most banks).

The Retail Lending Test primarily evaluates the distribution of a bank's loans in its assessment areas, and the outside retail lending area, within the retail lending categories that constitute "major product lines" for the bank within the geography. In a facility-based assessment area and the outside retail lending area, a "major product line" is any of the four categories of retail loans (closed-end home mortgages, small business loans, small farm loans, and, for majority-auto lenders, automobile loans) that comprises 15 percent or more of the bank's total lending in those product lines, by a combination of dollar amount and loan count, in that area. In a retail lending assessment area, a major product line is whichever product (closed-end home mortgages, small business loans, or both) triggers the relevant threshold to create the retail lending assessment area.

The distribution of a bank's loans in major product lines in a given area is generally evaluated across two dimensions: (1) a "geographic distribution" metric that evaluates the bank's proportion of originated and purchased loans to borrowers located in LMI census tracts in the area, and (2) a "borrower distribution" metric that evaluates the bank's proportion of originated and purchased loans that are to LMI borrowers, or to the smallest small businesses or small farms in the area overall, regardless of geography. For both metrics, the bank's performance is compared to (A) the comparable proportion reported by all reporting lenders in the area in a "market benchmark" and (B) local demographics in a "community benchmark."

Based on commenters' feedback, the agencies adjusted the standards for retail lending performance to make "Low Satisfactory," "High Satisfactory," and "Outstanding" conclusions on the test modestly more achievable than under the proposal.

Test 2: Retail Services and Products Test

The Retail Services and Products Test uses predominantly qualitative means, informed by quantitative metrics, to evaluate the availability and responsiveness of a bank's (a) retail banking services and (b) retail banking products.

The first Retail Services and Products sub-test, addressing the bank's retail banking services, considers:

(1) Branch availability and services;

(2) Remote service facilities; and

(3) Digital and other delivery systems.

First, the branch availability and services evaluation compares the distribution of a bank's branches in LMI census tracts to community and market benchmarks, with examiners retaining discretion about how to use that data to produce a conclusion. Examiners will evaluate a bank's record of opening and closing branches in LMI census tracts. Branches in certain underserved areas – i.e., branches in middle- and upper-income census tracts that serve LMI consumers, branches in distressed and underserved nonmetropolitan middle-income census tracts, and branches in Native Land Areas – will be considered favorably. Examiners will also evaluate hours of operation and services offered at branches in LMI census tracts as compared to other branches.

Second, the availability of remote service facilities (including ATMs) in a given facility-based assessment area is compared to community benchmarks based on income demographics. As compared to the proposal, the final rule permits additional consideration of remote service facilities in middle- and upper-income census tracts that serve LMI consumers, distressed or underserved nonmetropolitan middle-income census tracts, and Native Land Areas.

Third, for a large bank with more than $10 billion in assets, or a smaller large bank that does not operate through branches, digital and other delivery systems are evaluated at the institution level based on:

(i) Digital and other delivery system activity by individuals in LMI census tracts compared to that of middle- and upper-income census tracts, including usage and account openings;

(ii) The range of retail banking services and retail banking products offered through digital and other delivery systems; and

(iii) The bank's strategy and initiatives to serve LMI individuals through such systems.

The second Retail Products and Services sub-test evaluates the responsiveness of the bank's retail banking products, i.e., credit products and programs, and, for banks with more than $10 billion in assets, deposit products. In a change to the proposal, the final rule provides that this sub-test can only benefit a bank's conclusion.

Credit products and programs offered to LMI individuals, residents of LMI census tracts, and small businesses and small farms will be considered on a qualitative basis. Products such as low-cost education loans and loans offered through special purpose credit programs will receive favorable consideration.

Deposit products will be evaluated based on the availability and usage of such products that are responsive to LMI consumers' needs. To evaluate availability, examiners will consider the extent to which a bank offers deposit products with:

(i) Low-cost features, such as deposit products with no overdraft or insufficient funds fees, no low or minimum balance requirements, no or low monthly maintenance fees, or free or low-cost checking and bill payment services;

(ii) Features that facilitate broad functionality and accessibility, such as deposit products with in-network ATM access, debit cards for point-of-sale and bill payments, and immediate access to funds for customers cashing payroll, government, or bank-issued checks; or

(iii) Features that facilitate inclusive access by people without banking or credit histories or with adverse banking histories.

To evaluate usage, examiners will consider the number of responsive deposit accounts opened and closed in census tracts of differing income levels; the percentage of a bank's responsive deposit accounts compared to its total deposit accounts; marketing, partnerships, and other activities by the bank to promote awareness and use of responsive deposit accounts; and any other relevant bank-provided information.

Test 3: Community Development Financing Test

The Community Development Financing Test evaluates whether a bank meets community development financing needs in its facility-based assessment areas and elsewhere through community development loans and community development investments. Examiners will review the ratio of the dollar value of the bank's community development loans and community development investments to the bank's annual dollar volume of deposits, and compare that ratio to market benchmarks both locally and nationwide. The final rule leaves to examiner discretion how well a bank would need to do relative to the benchmarks to attain a particular conclusion on the test.

Examiners will also conduct a review of community development loans and community development investments to decide how impactful and responsive they are, drawing on an enumerated list of impact and responsiveness factors as well as any other performance context information. The enumerated impact and responsiveness factors include consideration of community development activities that serve areas with high or persistent poverty, activities that support minority depository institutions, women's depository institutions, low-income credit unions, or community development financial institutions; or are investments in projects financed with federal low-income housing tax credits or new markets tax credits.

The final rule adds to the proposed framework a Bank Nationwide Community Development Investment Metric for banks with more than $10 billion in assets. This metric measures the dollar volume of the bank's community development investments (excluding mortgage-backed securities) that benefit or serve all or part of the nationwide area, compared to the bank's nationwide deposits. Comparing the metric to a market benchmark can only contribute positively to the bank's overall Community Development Financing Test conclusion.

Test 4: Community Development Services Test

The Community Development Services Test reviews the extent to which a bank provides community development services and the impact and responsiveness of those services in satisfying community development needs. The test may incorporate certain quantitative metrics, such as:

(i) A bank's number of community development services attributable to each type of community development;

(ii) The capacities in which the board members or employees of a bank or its affiliates serve;

(iii) The total hours of community development services performed by

the bank; and

(iv) Other evidence that services are responsive to community development needs.

However, the test may also consider qualitative review of the impact and responsiveness of the community development services that benefit or serve the area. The agencies declined to adopt from the proposal a metric that would have measured the average number of community development service hours per full-time equivalent employee for a bank with more than $10 billion in assets.

As under the existing CRA regulations, community development services must pertain to the provision of financial services or the expertise of bank personnel. The agencies proposed loosening this requirement in nonmetropolitan (i.e., rural) areas, but ultimately did not adopt the change in the final rule.

An Institution-Level Performance Score

The four tests described above combine into a single overall institution-level performance score, with a weighting of 40 percent for the Retail Lending Test, 10 percent for the Retail Services and Products Test, 40 percent for the Community Development Financing Test, and 10 percent for the Community Development Services Test. This approach of weighting the retail-focused tests equally with the community development-focused tests departs from the weighting outlined in the proposal, which would have assigned more weight to the retail-focused tests.

Additionally, a large bank needs to receive at least a Low Satisfactory conclusion on the Retail Lending Test to receive a Satisfactory overall rating. A large bank with 10 or more assessment areas also must receive at least a Low Satisfactory conclusion in 60 percent of its assessment areas (by number) in order to receive a Satisfactory rating overall.

As is the case in the current CRA regulations, examiners could downgrade a bank's rating based on evidence of discriminatory or other illegal credit practices. The agencies had proposed to broaden this standard to consider discriminatory or other illegal practices unrelated to credit, but backed away from this change in the final rule.

The bank's final, institution-level rating can be "Outstanding," "Satisfactory," "Needs to Improve," or "Substantial Noncompliance," consistent with the existing CRA regulations.

THE FINAL RULE CLARIFIES AND TAILORS THE ACTIVITIES THAT RECEIVE CREDIT AS COMMUNITY DEVELOPMENT ACTIVITIES

The final rule provides that the agencies will establish and maintain a public, illustrative, and non-exhaustive list of qualifying community development

activities eligible for CRA credit. Additionally, a bank will be able to request from the agencies an advance determination that its activities qualify and should go on the list. The final rule also sets forth 11 community development purposes that warrant credit under the two Community Development tests. An activity generally is required to meet: a majority standard, generally meaning that a majority of the beneficiaries of an activity are LMI; bona fide intent standard, generally meaning that if the beneficiaries are not quantifiable, the bona fide intent of the activity is qualifying community development; involve a minority depository institution, women's depository institution, low-income credit union, or community development financial institution; or involve a low-income housing tax credit. However, some activities related to affordable housing that do not meet a majority standard or the other available standards could receive partial credit in proportion to the percentage of affordable housing units.

Notable examples of activities that would qualify as community development in the final rule include:

- Affordable housing, including through purchases of mortgage-backed securities;
- Disaster preparedness and weather resiliency;
- Financial literacy initiatives;
- Activities in Native Land Areas;
- Partnerships with minority depository institutions, women's depository institutions, low-income credit unions, and community development financial institutions; and
- Economic development activities in conjunction with or syndication with government programs, including direct small business loans meeting a size and purpose test.

Compared to the proposal, the final rule includes two notable changes.

First, the proposal would have provided that, for a housing initiative to be considered "affordable," rents generally could not exceed 30 percent of 60 percent of the area median income. In the final rule, the agencies loosened this criterion to be 30 percent of 80 percent of area median income.

Second, the final rule permits direct loans to small businesses to count as an economic development activity where "size" and "purpose" tests are satisfied. However, unlike under the existing CRA regulations, the loan must be "in conjunction or in syndication with" a government program. The preamble to the final rule suggests that an SBA 7(a) loan would qualify for credit if the size and purpose test are satisfied.

THE WHOLESALE AND LIMITED PURPOSE DESIGNATIONS HAVE BEEN CONSOLIDATED INTO A SINGLE LIMITED PURPOSE BANK DESIGNATION, AND THESE BANKS ARE SUBJECT TO EVALUATION BASED ON COMMUNITY DEVELOPMENT FINANCING ACTIVITIES WITH OPTIONAL CONSIDERATION OF COMMUNITY DEVELOPMENT SERVICES

The existing CRA regulations provide that "limited purpose" banks and "wholesale" banks can be evaluated under a tailored framework that focuses on community development activities. Under the final rule, the agencies combined the two designations into a single "limited purpose" bank designation, which is available to a "bank that is not in the business of extending closed-end home mortgage loans, small business loans, small farm loans, or automobile loans evaluated under [the Retail Lending Test] to retail customers, except on an incidental and accommodation basis, and for which a designation as a limited purpose bank is in effect." Existing limited purpose banks and wholesale banks are not required to re-apply for the designation. The final rule subjects limited purpose banks to a modified version of the Community Development Financing Test and, at the bank's option, an evaluation of community development services.

STRATEGIC PLANS REMAIN AN OPTION, WITH MORE CLARITY THAN UNDER THE PROPOSAL

Like the existing CRA regulations and the proposal, the final rule permits a bank to elect to be evaluated under a strategic plan in lieu of the generally applicable performance tests. Banks operating under a strategic plan could deviate from the four performance tests in certain respects, if justified, and the final rule is more explicit than the proposal regarding the ways in which these banks can depart from the generally applicable standards. For example, strategic plan banks may use alternative weighting of the four tests or component geographic scores. However, as is the case under the existing CRA regulations, the flexibility afforded to strategic plans comes with costs. A bank must consult with members of its communities when developing its plan, make its draft plan available for public comment, and obtain prior regulatory approval of the plan.

ONEROUS NEW DATA COLLECTION REQUIREMENTS APPLY TO LARGE BANKS, PARTICULARLY THOSE WITH MORE THAN $10 BILLION IN ASSETS

The final rule requires large banks to collect substantial data concerning deposits, retail loans, and community development activities, which will be used to evaluate performance in the quantitative parts of the final rule's four tests. A large bank with more than $10 billion in assets is required to collect the most granular data, including the county of each depositor, which determines

the bank's deposit base in each assessment area and the outside retail lending area and thereby influences the bank's CRA obligation in each area. Large banks with no more than $10 billion in assets could instead rely on the FDIC's existing Summary of Deposits data, which report the branches in which banks book their deposits, to determine their CRA obligations.

Banks operating under a strategic plan are subject to the same data collection and reporting standards as their size would dictate if they were evaluated under the generally applicable performance tests. Limited purpose banks are also subject to large bank data collection reporting requirements for community development loans and investments.

THE AGENCIES PLAN TO LEVERAGE SMALL BUSINESS LENDING DATA GATHERED UNDER THE CFPB'S SECTION 1071 FINAL RULE, IF AND WHEN THAT DATA BECOMES AVAILABLE

The Consumer Financial Protection Bureau's final rule[3] to implement Section 1071 of the Dodd-Frank Act requires covered financial institutions to collect and report to the CFPB data on applications for credit for small businesses, including small farms.

While the agencies had planned to use the Section 1071 definition of a "small business loan" and Section 1071 data in the CRA rules, the Section 1071 rule has been the subject of court challenges, and in October 2023 a district court issued a nationwide injunction halting its implementation. The CRA final rule's text therefore omits references to the Section 1071 rule. Instead, the CRA final rule maintains the definition of small business loan provided in the existing CRA regulations, which, consistent with the call report definition of loan to small business, includes any loan of $1 million or less to a business. The final rule also contains independent data collection requirements for small business loans.

The preamble to the final rule indicates that the agencies plan to amend the CRA regulations to transition to the Section 1071 definition of a small business loan and Section 1071 data after they become available. Under the Section 1071 rule, a small business loan is an extension of business credit to a small business – which is generally a business with gross annual revenue of $5 million or less – other than trade credit, HMDA-reportable transactions, insurance premium financing, public utilities credit, securities credit, or incidental credit, without any loan amount threshold.

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[3] https://www.consumerfinance.gov/rules-policy/final-rules/small-business-lending-under-the-equal-credit-opportunity-act-regulation-b/.