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Agencies Finally Approve Jointly Proposed Rule to Modernize CRA Regulations*

On Tuesday, October 24, 2023, the Federal Reserve, FDIC, and OCC approved a rule (Final Rule) that will jointly finalize a six-year saga to modernize the regulations that implement the 46-year old Community Reinvestment Act (CRA). The Final Rule, which generally adopts the May 2022 proposed rule, is the first major update to the CRA regulations since 1995, other than the OCC rule that was rescinded a few years ago.

One of the ways the CRA achieves its designed purpose of encouraging banks to meet the credit needs of its communities, including low- or moderate-income neighborhoods, is by requiring the agencies to evaluate and publicly report a bank's CRA-related retail banking and community development performance. The Final Rule updates the agencies' performance evaluation framework and criteria, expands areas of assessment, establishes standardized performance tests and metrics, and clarifies community development activity and reportable loan definitions.

Evaluation Framework and Criteria. The Final Rule continues to use a framework that is based on a bank's asset size and business model. In other words, the agencies apply different performance standards to banks of different sizes and activities. The Final Rule classifies banks with less than \$600 million in assets as of December 31 of the prior two calendar years as "small," banks with assets of at least \$600 million and less than \$2 billion over the same time period as "intermediate," and banks with assets of at least \$2 billion as "large." It also revises the definition of limited purpose bank to include both limited purpose banks and wholesale banks.

The Final Rule has the agencies utilize a combination of seven performance tests based on whether a bank is small, intermediate, large, or limited purpose. Small banks will default to a Small Bank Lending Test evaluation or could opt-in to a new Retail Lending Test. Intermediate banks will be evaluated under the Retail Lending Test and either an Intermediate Bank Community Development Test or a new Community Development Financing Test. Large banks will be separately evaluated under the Retail Lending Test, Retail Services and Products Test, Community Development Financing Test, and Community Development Services Test. Limited purpose banks will be evaluated under the aptly named Community Development Financing Test for Limited Purpose Banks Test. Finally, banks of all sizes would continue to have the option to be evaluated under an approved strategic plan.

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For each applicable test, the agencies will make determinations based on a bank's performance in its facility-based assessment area(s). For the Retail Lending Test, the agencies will also make conclusions based on a bank's performance in retail lending assessment areas and areas outside their retail lending assessment areas, as applicable. If necessary, those individual determinations will be weighted and combined to determine a bank's CRA rating as either "Outstanding," "Satisfactory," "Needs to Improve," or "Substantial Noncompliance." The Final Rule will continue to allow the agencies to downgrade a bank's CRA rating based on discriminatory or illegal credit practices.

Assessment Areas. The Final Rule maintains the current approach of delineating a bank's assessment areas and will now also take into account a bank's use of technology, such as mobile banking and online lending. Banks will still be required to draw assessment areas around their physical deposit-taking locations ("facility-based assessment areas"), and some banks will also draw new "retail lending assessment areas," based on lending thresholds outside of their facility-based assessment area(s). The Final rule continues to prohibit discriminatory assessment area boundaries.

Retail Lending Test. The Final Rule assesses a bank's retail lending to low- or moderate-income (LMI) individuals, small businesses, small farms, and in LMI census tracts by primarily evaluating its home mortgage, multifamily, small business, and small farm loan originations and purchases within its facility-based assessment areas and, as applicable, retail lending assessment areas and outside retail lending area.

Under the Final Rule, the retail lending test measures both lending volume and distribution. A bank's lending volume will be measured as a ratio of qualified lending to its total deposits within its facility-based assessment area(s), and that ratio will be compared against an aggregate ratio for certain reporting banks in the same assessment area. A bank's lending distribution will be evaluated based on LMI geographic and borrower lending distribution tests for each of its major retail lending product lines (closed-end mortgage loans, small business loans, and small farm loans, for most banks). Agencies will measure a bank's LMI lending distribution performance against established benchmarks and other factors to make a conclusion such as "Satisfactory."

Community Development. In evaluating a bank's CRA performance under the applicable performance tests, the agencies are to consider a bank's community development loans, investments, and services. The Final Rule expands qualifying community development activities to include eligible activities regardless of location. It clarifies qualifying community development activities by defining eleven community development categories as well as creating publicly available illustrative lists of qualifying activities and a process for seeking confirmation that a community development activity is a qualifying activity.

Interplay with Section 1071 of the Dodd-Frank Act. The Final Rule revises the terms small business loan and small farm loan to be consistent with the definitions of small business in the CFPB's Section 1071 rule. It requires the agencies to transition to using a large bank's reported Section 1071 small business and small farm lending data once that data become available.

Important Dates. At nearly 1,500 pages including the supplementary information, the Final Rule will likely be published jointly in the Federal Register in time to become effective April 1, 2024. However, most of the Final Rule's definitions and requirements won't become applicable until January 1, 2026. New data reporting requirements will apply as of January 1, 2027, with banks subject to the reporting requirements first reporting by April 1st of that same year.

Banks can expect additional guidance from the agencies, including updated examination procedures, data reporting guides, and submission templates. BCG members can also expect additional analysis and training on the rule in the coming months. In the meantime, for more information contact Harijot “Harry” Khalsa at **HKhalsa@ABLAWYERS.COM** and Andrew Litchy at **ALitchy@ABLAWYERS.COM**, or at 800-742-3600 with questions.