

# The Banking Law Journal

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# Community Reinvestment Act Rule Overhaul Finalized by U.S. Banking Regulators

*By Matthew Bisanz, Kris D. Kully, Tori K. Shinohara, Jeffrey P. Taft and  
Kerri Elizabeth Webb\**

*Several banking agencies have finalized an overhaul of the regulations implementing the Community Reinvestment Act. This article provides background on the rulemaking process and a high-level summary of the final rule.*

The Federal Deposit Insurance Corporation (FDIC), the Federal Reserve Board (FRB), and the Office of the Comptroller of the Currency (OCC) (the Agencies) have finalized an overhaul of the regulations implementing the Community Reinvestment Act (CRA) (the Final Rule).<sup>1</sup> The Final Rule is the result of a coordinated interagency effort and drastically changes how all but the smallest banks will be evaluated for compliance with the CRA.

The Final Rule is the culmination of a rulemaking process that initiated five years ago to modernize the CRA regulations. The result is an incredibly complex regulatory scheme, with the version to be published in the Federal Register coming in at 1,494 pages and 651,627 words, including background and section-by-section analysis—“by far the longest rulemaking the FDIC has ever issued,” according to FDIC Vice Chairman Travis Hill.<sup>2</sup> The text of the regulation itself is over 60,000 words.

The Final Rule becomes effective on April 1, 2024, but there is a multiyear phase-in. This article provides background on the rulemaking process and a high-level summary of the Final Rule.

## **BACKGROUND**

The CRA, passed in 1977, generally requires insured depository institutions to participate in investment, lending, and service activities that help meet the

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<sup>1</sup> Federal Register Notice: Community Reinvestment Act, available at: <https://www.federalreserve.gov/aboutthefed/boardmeetings/files/frn-cra-20231024.pdf>. The Agencies have also issued summaries and fact sheets on the Final Rule, available at: <https://www.federalreserve.gov/consumerscommunities/community-reinvestment-act-final-rule.htm>; <https://www.fdic.gov/news/press-releases/2023/pr23086.html>; and <https://www.occ.gov/news-issuances/bulletins/2023/bulletin-2023-32.html#:~:text=Key elements of the final, and Community Development Services Test.>

<sup>2</sup> Statement by Vice Chairman Travis Hill on the Final Rule on Community Reinvestment Act Regulations (October 24, 2023), available at: <https://www.fdic.gov/news/speeches/2023/spoct2423c.html>.

credit needs of their designated assessment areas—particularly low- and moderate-income (LMI) communities and small businesses and farms. Insured depository institutions receive a rating from the banking regulators based on their performance. The CRA also requires the U.S. banking regulators to:

- Encourage banks to meet the credit needs of the communities that they serve in a safe and sound manner, and evaluate their record of doing so.
- Take that record into account when evaluating certain banking applications.
- Report to Congress the actions they have taken to carry out their CRA responsibilities.

The U.S. banking regulators issued the first set of regulations to implement the CRA in 1978 and revised them in 1995 and 2005, with the most substantive interagency update occurring in 1995. Given the significant changes to the business of banking, and the methods of offering financial products and services (e.g., less reliance on physical locations for certain banks) since the substantive changes in 1995, the CRA regulations had become outdated. In recent years, the regulators have taken divergent approaches to revising the CRA regulations, with the OCC briefly and unilaterally issuing an amendment in May 2020. The OCC later rescinded that amendment, and the regulators announced their commitment to work together in order to strengthen and update the CRA regulations, providing a more consistent framework across all banks.

Although the Final Rule is an interagency effort, the Final Rule's passage was not unanimous. Notably, two members of the FDIC Board of Directors, Vice Chair Travis Hill and Director Jonathan McKernan, and one Federal Reserve Board member, Michelle Bowman, voted against the Final Rule. Their cited disagreements included the Final Rule's complexity, questions about the Agencies' statutory authority to issue portions of the Final Rule, and whether the Final Rule's costs will outweigh its benefits.<sup>3</sup>

## THE FINAL RULE

The Final Rule comprehensively revises the CRA regulations. In short, the Agencies stated that the Final Rule seeks to accomplish the following goals:

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<sup>3</sup> Id.; Statement by Jonathan McKernan, Director, FDIC, Board of Directors on the Final Rule Implementing the Community Reinvestment Act (Oct. 24, 2023), available at: <https://www.fdic.gov/news/speeches/2023/spoct2423f.html>; Statement on the Community Reinvestment Act Final Rule by Governor Michelle W. Bowman (Oct. 24, 2023), available at: <https://www.federalreserve.gov/aboutthefed/boardmeetings/files/bowman-statement-20231024.pdf>.

- Encourage banks to expand access to credit, investment, and banking services in LMI communities.
- Adapt to changes in the banking industry, including mobile and online banking.
- Provide greater clarity and consistency in the application of the CRA regulations.
- Tailor CRA evaluations and data collection to bank size and type.

The Final Rule's major changes to the existing CRA regulations are discussed below, as well as differences from the Agencies' Proposed Rule issued in 2022.

### **Bank Size**

As under the current CRA regulations and the Proposed Rule, the Agencies will continue to apply different tests depending on a bank's asset size and business model. For all but the smallest banks, the Agencies have developed new tests to evaluate CRA performance:

- Large banks with \$2 billion or more in assets will be evaluated under a Retail Lending Test, a Retail Services and Products Test, a Community Development Financing Test, and a Community Development Services Test (discussed below).
- Intermediate banks (those with assets of at least \$600 million and less than \$2 billion) will be evaluated under the new Retail Lending Test and under either the current Intermediate Bank Community Development Test, or, at the banks' option, the new Community Development Financing Test.
- Small banks (those with assets of less than \$600 million) will be evaluated under the current Small Bank Lending Test or, at the banks' option, the new Retail Lending Test.
- Limited purpose banks (now defined to include wholesale banks, which have been eliminated as a separate category) will be evaluated under a modified Community Development Financing Test for Limited Purpose Banks.<sup>4</sup>
- Banks of all sizes can still request an evaluation under an approved strategic plan. The Final Rule provides some additional clarity and flexibility from the Proposed Rule on how banks can develop a strategic

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<sup>4</sup> Limited purpose bank means a bank that offers only a narrow product line (such as credit card or motor vehicle loans) to a regional or broader market and for which a designation as a limited purpose bank is in effect.



plan, although this option remains subject to community engagement and regulatory approval requirements.

**Applicability of Performance Tests Under Draft Final Rule**

<b>Small Banks</b>	Small Bank Lending Test (default) or Retail Lending Test (opt-in)			
<b>Intermediate Banks</b>	Retail Lending Test		Intermediate Bank Community Development Test (default) or Community Development Financing Test (opt-in)	
<b>Large Banks</b>	Retail Lending Test	Retail Services and Products Test	Community Development Financing Test	Community Development Services Test
<b>Limited Purpose Banks</b>	Community Development Financing Test for Limited Purpose Banks			

As under the Proposed Rule, the Final Rule requires inclusion of a bank’s “operations subsidiaries” in the evaluation of the institution’s CRA performance.<sup>5</sup>

**Geographic Assessment Focus**

The CRA remains a largely geographical regime. While the statute intends for banks to serve their “entire community,” the Agencies have elaborated on that term by requiring banks to delineate one or more metropolitan areas or contiguous political subdivisions where they have main or branch offices or deposit-taking remote service facilities, and surrounding areas (census tracts) in which they originated or purchased a substantial portion of their loans. The Agencies have revised the current assessment area framework by requiring all evaluated banks to continue to delineate facility-based assessment area(s), and requiring large banks to delineate a new area, referred to as retail lending assessment area(s). In addition, retail lending performance of large banks, and certain intermediate banks, will be evaluated in their outside retail lending areas. The Final Rule addresses those delineations in an effort to recognize modernization in the industry, provide additional clarity, and tailor standards for differences in bank size, business models, and local conditions.

- *Facility-Based Assessment Areas:* The Agencies faced the task of defining which facilities—and thus which geographies—should trigger banks’ lending, service, and community development obligations. This aspect

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<sup>5</sup> The Final Rule defines an operations subsidiary as “an organization designed to serve, in effect, as a separately incorporated department of the bank, performing, at locations at which the bank is authorized to engage in business, functions that the bank is empowered to perform directly,” which may not align with other regulatory definitions.

of the regime can affect bank determinations of where it will locate facilities, as the bank will then be obligated to serve that area for purposes of CRA compliance.

The statute requires the Agencies, in the written evaluation of a bank, to present conclusions separately for each metropolitan area in which the bank maintains a branch, and for the remainder of the nonmetropolitan area of the state if the bank maintains one or more branches in such nonmetropolitan area. Under the Final Rule, a bank's facility-based assessment area(s) must consist of a single metropolitan statistical area (MSA), one or more contiguous counties within an MSA, or one or more contiguous counties within a state's non-metropolitan area. Such an area may not extend beyond an MSA boundary or a state boundary, unless the area is located within a multistate MSA. However, the Agencies indicate that examiners will take certain factors (like geographic barriers in large counties) into consideration when evaluating a large bank's performance in such a facility-based assessment area. An intermediate or a small bank may include only the portion of a county that it can reasonably be expected to serve, subject to certain limitations. However, an area that includes a partial county must consist of contiguous whole census tracts.

A bank's facility-based assessment areas may not reflect illegal discrimination, and may not arbitrarily exclude low- or moderate-income census tracts, taking into account the bank's size and financial condition. However, the Agencies declined to define when such an arbitrary exclusion is taking place.

- *Retail Lending Assessment Areas:* As in the Proposed Rule, large banks will be newly required to delineate a retail lending assessment area in an MSA or the nonmetropolitan areas of a state in which the bank has a concentration of closed-end home mortgage or small business lending<sup>6</sup> outside of its facility-based assessment area(s). This area is intended to be separate and distinct from a bank's facility-based assessment area, recognizing that the proliferation of online lending and other non-branch-based delivery channels increasingly allows a bank to serve a community without a facility.

In that vein, and in consideration of public comments, the Final Rule exempts large banks that would have a substantial overlap between their facility-based and retail lending assessment areas. Specifically, large banks would

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<sup>6</sup> Note that the Agencies have abandoned a plan to conform the definition of "small business loan" with the CFPB's definition under its Section 1071 rule, possibly due in part to legal challenges to the Section 1071 rule. Instead, the Final Rule retains the existing definition of "small business loan" under the existing CRA regulations, which includes any loan of \$1 million or less to a business.

be relieved of this additional compliance burden if they conduct more than 80% of their retail lending within facility-based assessment areas (based on a combination of loan dollars and loan count; i.e., the average of the two percentages).

In addition, as compared to the Proposed Rule, the Final Rule increases the loan count thresholds, and trims back the product types, that trigger the retail lending assessment area delineation requirement to at least 150 closed-end home mortgage loans, or at least 400 small business loans in each year of the prior two calendar years.<sup>7</sup>

The Agencies estimate that, as compared to the Proposed Rule, the Final Rule cuts in half the number of banks and assessment areas to which this retail lending evaluation will apply.

The retail loans included in the calculation are:

- The bank's originated and purchased home mortgage loans;
- Multifamily loans;
- Small business loans;
- Small farm loans; and
- Automobile loans.

The Final Rule includes in a bank's evaluation the activities of a bank's operations subsidiaries or operating subsidiaries, including loans, investments, services, and products of a bank's operations subsidiaries or operating subsidiaries, unless the bank's subsidiary is independently subject to the CRA. Under the Final Rule, the Agencies will continue to consider the loans, investments, services, and products of affiliates of a bank that are not operations subsidiaries or operating subsidiaries, at the bank's option. This optional consideration is subject to certain requirements.

- *Outside Retail Lending Area:* The Agencies will evaluate the retail lending performance of large banks, certain intermediate banks, and certain opt-in small banks in areas that are outside the banks' facility-based and retail lending assessment areas, including in certain nonmetropolitan counties. Evaluation of intermediate banks in their outside retail lending areas is mandatory if the intermediate bank conducts a majority of its retail lending outside of its facility-based assessment areas. This will allow the Agencies to evaluate a bank's retail

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<sup>7</sup> The Proposed Rule would have set those thresholds for a large bank at an annual lending volume of at least 100 home mortgage loan originations (including both open- and closed-end loans), or at least 250 small business loan originations.

lending that is too dispersed to be evaluated within a specific geographic area, or that does not meet the lending thresholds described above. The Agencies hope this assessment will aid in recognizing the expanded role of mobile and online banking.

In a change from the Proposed Rule, the Final Rule: (1) adjusts the standard used to determine when an intermediate bank's outside retail lending area is evaluated on a mandatory basis, and applies the same standard to a small bank that opts to be evaluated under the Retail Lending Test; (2) permits an intermediate or small bank that does not meet this standard to opt to have its outside retail lending area evaluated; and (3) tailors the proposed geographic standard for outside retail lending areas to exclude those nonmetropolitan counties in which a bank did not originate or purchase any closed-end home mortgage loans, small business loans, small farm loans, or automobile loans (if automobile loans are a product line for the bank).

### Tests

The Final Rule revises several existing tests, and creates new ones to replace those under the current CRA regulations:

- *Retail Lending Test.* The Final Rule revises the existing Retail Lending Test to evaluate how banks are serving LMI borrowers, small businesses and small farms in their facility-based assessment areas and, as applicable for certain large banks and intermediate banks, in their retail assessment areas and outside retail lending areas. The test includes two sets of metrics. First, the Retail Lending Volume Screen measures the volume of a bank's lending relative to its deposit base in its facility-based assessment area and compares that ratio to the aggregate ratio for all reporting banks in the same facility-based assessment area. Second, the Agencies will evaluate the geographic distribution and borrower distribution of a bank's major product lines in all assessment areas using a series of metrics and benchmarks.

In response to comments on the Proposed Rule, the Final Rule adjusts some of the performance multipliers to make favorable performance conclusions more attainable. The Final Rule also reduces the number of evaluated product lines from six, as proposed, to three for most banks. The Final Rule also only requires evaluation of a bank's automobile loans if such loans represent a majority of the bank's retail lending, or at the bank's option.

- *Retail Services and Products Test.* For large banks, this new test evaluates the availability of a bank's retail banking services and retail banking products, as well as the responsiveness of those services and products to LMI communities, small businesses, and small farms, including for

some banks, the availability of digital and other delivery systems. This test is largely unchanged from the Proposed Rule, although includes some adjustments, including incorporating benchmarks to evaluate the availability of a bank's branch and remote service facilities. Another key change from the Proposed Rule is that the responsiveness portion of the test will only positively contribute to a bank's rating. For large banks with assets less than \$10 billion, the Agencies will not evaluate the availability and usage of responsive deposits products, except at the bank's option.

- *Community Development Financing Test.* This new test will combine the current evaluations of community development loans and investments in a community development financing metric. It also will include an impact and responsiveness review to determine whether community development loans, investments, and services are particularly impactful or responsive. This could be used to recognize the importance of affordable housing and community development contributions of Low-Income Housing Tax Credit and New Markets Tax Credit investments. This test will also include a metric for banks with assets greater than \$10 billion to measure the bank's community development investments relative to deposits, a metric which can only contribute positively to the test's conclusion. This will allow examiners to evaluate bank investments under the Low-Income Housing Tax Credit and the New Markets Tax Credit programs.

Limited purpose banks will be evaluated under a modified Community Development Financing Test, which will include an institution level-metric that measures a bank's volume of activities relative to its capacity.

- *Community Development Services Test.* This new test for large banks will be a primarily qualitative assessment of the bank's community development service activities. Unlike in the Proposed Rule, volunteer services in all areas must be related to the provision of financial services or expertise of bank staff and must have a community development purpose in order to be considered. The Final Rule also eliminates a requirement under the Proposed Rule that would have measured the hours of community development services activity per full-time equivalent bank employee.

Limited Purpose Banks have the option to have examiners consider community development service activities that would qualify under the Community Development Services Test.

- *Strategic Plan.* The Final Rule retains the strategic plan option as an alternative method of evaluation with some minor changes. Under this

alternative, banks of any size may elect to be evaluated under a strategic plan that sets out measurable, annual goals for lending, investment, and service activities in order to achieve a “Satisfactory” or an “Outstanding” rating. A strategic plan must be developed with community input and approved by the appropriate Federal financial supervisory agency.

### **Performance Score and Assigned Ratings**

The Final Rule revises the process for assigning ratings for a bank’s overall performance. For each performance test, banks will be assigned one of the following five conclusions: “Outstanding,” “High Satisfactory,” “Low Satisfactory,” “Needs to Improve,” and “Substantial Noncompliance.”<sup>8</sup>

The conclusions for the various tests will be combined to assign the bank an overall CRA rating of “Outstanding,” “Satisfactory,” “Needs to Improve,” or “Substantial Noncompliance.” The combination would reflect specific weights attributed to each performance test that vary depending on the bank’s asset size:

- For large banks, the heaviest weight will be allocated to the Retail Lending and Community Development Financing Tests (40% each), with lower weights attributed to the Retail Services and Products and the Community Development Services Tests (10% each). These weights were adjusted from the Proposed Rule in response to comments that the Community Development Financing Test was underweighted.
- For intermediate banks, tests are weighted equally between the Retail Lending Test and the status quo community development test (or Community Development Financing Test, when selected by the bank).

Evidence of discriminatory or illegal credit practices by bank subsidiaries will continue to be factored into a bank’s rating.<sup>9</sup> In the past, this has caused certain banks to have their rating dropped by one—or, in certain extreme situations—two categories. Also, regulators will continue to weigh a bank’s CRA performance when considering certain applications, including those for a branch opening; a merger, consolidation or acquisition; a main office or branch relocation; a deposit insurance request; and transactions subject to the Bank Merger Act and Bank Holding Company Act. Notably, an institution with a CRA rating below “Satisfactory” could be restricted from engaging in certain activities until its next CRA examination.

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<sup>8</sup> For small banks evaluated under the Small Bank Lending Test, the Agencies will assign one of four conclusions: Outstanding,” “Satisfactory,” “Needs to Improve” or “Substantial Noncompliance.”

<sup>9</sup> The Final Rule adds the following to the listed discriminatory or other illegal practices: violations of the prohibition against unfair, deceptive, or abusive acts or practices; violations of the Military Lending Act; and violations of the Servicemembers Civil Relief Act. The Final Rule eliminates the proposal that illegal non-credit practices also be considered.

While the overall CRA ratings available to banks have not changed in the Final Rule, there are concerns that banks may have a more difficult time obtaining an outstanding or satisfactory rating.<sup>10</sup>

### **Community Development Categories**

The Final Rule defines 11 community development categories:

- Affordable housing;
- Economic development activities;
- Community supportive services;
- Revitalization or stabilization activities;
- Essential community facilities;
- Essential community infrastructure;
- Recovery activities that promote the recovery of a designated disaster area;
- Disaster preparedness and weather resiliency activities;
- Qualifying activities in Native Land Areas;
- Financial literacy; and
- Activities with Minority Depository Institutions, Community Development Financial Institutions, women's depository institutions, and low-income credit unions.

The Agencies made some key changes to qualifying community development activities from the Proposed Rule. For one, the Proposed Rule would have required that qualifying affordable housing initiatives have rents 30% or lower of 60% of the area median income. The Final Rule more flexibly permits rents of 30% or lower of 80% of the area median income. The Final Rule also expands economic development activities to include direct loans to small businesses and small farms made in conjunction or in syndication with government programs, so long as the activity meets a size and purpose test. Notably, the Agencies cited a Small Business Administration 7(a) loan as a potentially qualifying activity, provided the loan otherwise meets the applicable criteria.

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<sup>10</sup> Statement on the Community Reinvestment Act Final Rule By Governor Michelle W. Bowman (“The final rule would also make it much more difficult for banks to maintain existing CRA ratings without making significant changes to their current activities. As described in the materials before the Board today, based on changes to the retail lending test alone, nearly 10 percent of banks would be rated ‘Needs to Improve’ based on data from 2018 to 2020.”) (Oct. 24, 2023), available at: <https://www.federalreserve.gov/aboutthefed/boardmeetings/files/bowman-statement-20231024.pdf>.

The Agencies will develop and maintain a public list of examples of activities that qualify for community development consideration and incorporate a process through which banks can confirm whether a particular loan, investment or service may be eligible for community development consideration.

### **Data Collection and Reporting**

The Final Rule includes extensive data collection and reporting requirements that vary depending on a bank's size, although the Final Rule does not change data collection and reporting requirements for small and intermediate banks. Large banks, however, are subject to updated and expanded data collection, maintenance, and reporting requirements. Large banks with over \$10 billion in assets will be subject to still more data requirements.

### **Compliance Timeline**

Although the Final Rule takes effect on April 1, 2024, banks will not become subject to most of the requirements, including new assessment area requirements and performance tests, until January 1, 2026. Banks will not be required to comply with the new data reporting requirements until 2027. The Agencies doubled the compliance timelines for many key requirements from the Proposed Rule in response to comments.

The Agencies intend to issue supervisory guidance, including examination procedures, as well as conduct outreach and training on the Final Rule. In addition, the Agencies intend to develop data reporting guidance, technical assistance materials, templates, and other tools as necessary to achieve consistency and efficiency. The Agencies also plan to develop data tools using reported loan data to provide more transparency into performance standards.

### **TAKEAWAYS**

The Final Rule represents the most substantive interagency updates to the CRA in over 25 years. However, as one of the Final Rule's dissenters pointed out, portions of the rule are still unfinished, including the methodology to combine the various test benchmarks and metrics into a performance conclusion.<sup>11</sup> Furthermore, the Final Rule is being issued as the Agencies propose updates to their capital rules which could have an impact on bank CRA programs.

The updated regulations are incredibly complex, and it will take substantial time for the industry to comprehend them, not to mention satisfy the new

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<sup>11</sup> Statement by Jonathan McKernan, Director, FDIC, Board of Directors on the Final Rule Implementing the Community Reinvestment Act (Oct. 24, 2023), available at: <https://www.fdic.gov/news/speeches/2023/spoct2423f.html>.



compliance and performance requirements. Although the initial compliance dates are years away, banks and other stakeholders will need all the time allotted to implement the 1,500 page Final Rule.