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New CRA Rule Amendments Encourage Institutions to Provide Foreclosure Relief

On December 20, 2010, the Office of the Comptroller of the Currency, the Board of Governors of the Federal Reserve System, the Federal Deposit Insurance Corporation, and the Office of Thrift Supervision (collectively, the Agencies) published a joint final rule (Final Rule) expanding the category of community development activities that qualify for Community Reinvestment Act (CRA) credit to include loans, investments, and services that support, enable, or facilitate projects or activities under a recent federal program designed to address the home mortgage and foreclosure crisis. The Final Rule becomes effective on January 19, 2011.

As financial institutions know, the CRA requires the Agencies to assess the record of each insured depository institution in helping to meet the credit needs of its entire community, including low- and moderate-income neighborhoods, consistent with the safe and sound operation of the institution, and to take that record into account when evaluating various expansion activities by the institution. Among other things, financial institutions may receive credit in their CRA examinations for community development loans, qualified investments, and community development services which have a primary purpose of "community development." As summarized further below, the Final Rule expands what can count as "community development" activities.

Summary of Final Rule's Expansion in Community Development Activities

Recognizing the need to provide emergency assistance to communities affected by the high level of foreclosures, Congress established the Neighborhood Stabilization Program (NSP) in 2008. The program initially provided emergency funds for the redevelopment of abandoned and foreclosed homes, totaling nearly $4 billion, to states and localities with the greatest need for such funds. In 2009, an additional $2 billion in NSP funding was provided not only to states and local governments, but also to non-profit organizations through a competitive bidding process administered by the United States Department of Housing and Urban Development (HUD).

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More NSP funds, totaling $1 billion, were set aside in the Dodd-Frank Wall Street Reform and Consumer Protection Act (Dodd-Frank Act). HUD has established a formula for deciding how to allocate the additional funds. It determines the states and localities with the greatest need based on the number and percentage of home foreclosures, the number and percentage of homes financed by a subprime mortgage-related loan, and the number and percentage of homes in default or delinquency in each state or unit of local government. On September 8, 2010, HUD announced the allocation of $970 million in funds to 283 grantees nationwide.

The Final Rule allows institutions to receive CRA credit for supporting, enabling, or facilitating NSP-eligible activities in the geographic areas targeted in approved NSP plans. NSP-eligible activities are projects or activities that use the NSP funds to:

1. Establish financing mechanisms for purchase and redevelopment of foreclosed upon homes and residential properties;
2. Purchase and rehabilitate homes and residential properties that have been abandoned, or foreclosed upon, in order to sell, rent, or redevelop such homes and properties;
3. Establish and operate land banks for homes and residential properties that have been foreclosed upon;
4. Demolish blighted structures; and
5. Redevelop demolished or vacant properties.

The Dodd-Frank Act requires that at least 25 percent of the NSP funds received by each grantee must be used with respect to low-income individuals and families, and that NSP funds *may not be* used with respect to upper-income individuals and families. However, unlike most CRA activities, the community development activities covered by the Final Rule can benefit *middle-income* individuals and geographies in addition to low- and moderate-income individuals and geographies. The CRA regulations define "middle-income" as "an individual income that is at least 80 percent and less than 120 percent of the area median income or a median family income that is at least 80 percent and less than 120 percent in the case of a geography."

Thus, under the revised definition of "community development," a financial institution will receive favorable CRA consideration, for example, for a donation of other real estate owned properties to non-profit housing organizations in eligible middle-income, as well as low- and moderate-income geographies. Additionally, institutions will receive favorable CRA credit, for example, if they provide financing for the purchase and rehabilitation of foreclosed, abandoned, or vacant properties in targeted areas.

Finally, under the current CRA regulations, an institution is evaluated under the current CRA rules primarily on how it helps meet the credit and community development needs of its CRA assessment area(s). The Final Rule provides that an institution that has adequately addressed the community development needs of its assessment area(s) may receive favorable CRA consideration for NSP-eligible activities that are *outside* of its assessment area(s).

While most CRA activities do not have termination dates, the Final Rule provides that NSP-eligible activities will receive favorable consideration if conducted no later than two years after the last date that funds appropriated for the program are required to be spent by the grantees. The Agencies have not set forth a specific termination date; however, they indicated that they will provide reasonable advance notice to institutions in the Federal Register regarding termination of the rule once a specific date has been determined.

The rule, in its proposed form, was welcomed by commenters because it provides a CRA incentive for institutions to engage in activities that stabilize communities affected by foreclosures. This incentive works together with the funding provided by the NSP towards the goal of helping to revive areas that have been devastated by the foreclosure crisis.

Furthermore, we are likely to see further changes to the CRA rules in the near future. The preamble to the Final Rule notes that the Agencies have begun a regulatory

review of the CRA rules generally, and that during that process they will carefully consider any comments received that may recommend further changes to, among other things, the definition of "community development." In addition, the Agencies have indicated that they will consider issuing additional guidance in connection with a future revision of the Interagency Questions and Answers Regarding Community Reinvestment or examination procedures to the extent that additional guidance may be needed regarding the provision of CRA credit for activities outside an institution's assessment area(s).

Arnold & Porter LLP is available to respond to questions raised by the Final Rule. We can assist you in determining how the Final Rule may affect your business and industry. For further information, please contact your Arnold & Porter attorney or:

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