Communities & Banking explores the emerging use of equity capital as a tool for community and economic development. We offer three related articles:

1. **Wall Street on Main Street**
2. **Community Development Venture Capital and the New CRA**
3. **Where Social and Financial Goals Meet**
4. **New England's Enterprise Communities: An Experiment in Economic Revitalization**

Susan Cournoyer examines the challenges of implementing this economic development initiative.

Compliance Q&A
From twelve factors to three tests: Large institutions transition to the new CRA.

Information Exchange
The Boston Fed’s Community Information Resource Center

Why Equity Capital?
For some time community development professionals have recognized the need for equity financing. Debt capital, while available, often does not meet the financing needs of many small ventures. Equity capital is especially important for enterprises in higher-growth market areas because it provides the patient capital necessary for businesses to establish themselves and to grow.

Nick Smith, president of the nationwide Community Development Venture Capital Alliance (CDVCA), notes that community development venture capital “grew out of the resolve of regional leadership to diversify local economies, partly through home-owned and home-grown businesses.” Working alongside other economic development programs, equity capital programs address community problems related to the large scale of financial and business activities. “Through community development venture capital, we’re intervening in the hopes of creating smaller-scale businesses that have historically been at the center of flourishing, empowered communities.”

Competing Goals?
Community development and traditional venture capital share similar characteristics. Both look for high-growth market areas. Both look for potentially successful enterprises. Both seek well-thought-out business plans. And both require highly trained professionals to evaluate and manage investments.
Yet CDVC professionals define their mission very differently than do traditional venture capitalists: They evaluate success in social as well as financial terms. "We are using this tool to effect social and economic change," says BCLF Ventures' Managing Director, Halim Dyer, "we look holistically at communities, and at the lives of individuals." Along with financial returns, BCLF Ventures seeks to create respectable employment, deliver needed goods and services, generate positive economic activity, and establish links between lower-income communities and the broader economy.

When considering financial returns, a fund manager addresses the need for the fund to be financially self-sustaining as well as its ability to attract investors. When considering social returns, the manager looks at the number and quality of the jobs, the impact on the environment, and whether the enterprise provides needed goods or services.

Because CDVC professionals pursue dual goals, they must often compromise financial returns for social impact. Practitioners acknowledge this tension but contend that both are critical to creating sustainable economic development. Meriwether Jones of the Aspen Institute depicts the compromise inherent in pursuing such a "double bottom line." (See Figure 1.)

Figure 1. A defining moment for any fund will be to decide what mix of community development and financial outcomes it will seek, deal by deal, and for the resulting portfolio of deals.

Jones' conceptualization furthers understanding of the potential trade-offs associated with seeking both financial and social returns. He emphasizes that practitioners and investors alike should look to maximize the total combined return of each investment: "A defining moment for any fund will be to decide what mix of community development and financial outcomes it will seek, deal by deal, and for the resulting portfolio of deals."

At the business management level, trade-offs may or may not exist as firms make policy decisions. For example, Nathaniel Henshaw, President of Coastal Ventures, cites questions of whether a firm should offer employee health insurance benefits. An affirmative decision would increase a company's costs, and therefore affect its bottom line. At the same time, however, that decision may also increase a firm's ability to attract and keep well-qualified employees, a factor often critical to delivering competitively priced, high-quality products.

But sometimes an enterprise's viability hangs on such a decision, as, for example, when offering health insurance benefits would be financially damaging to the firm. It is in these times that are especially trying for social investors as they perform their voting role on a firm's board of directors and advise the business on broad policy matters. "A situation like that is always difficult, but I base my decision on what I believe is in the ultimate best interest of society," Henshaw states.
Managing Risks

Equity investing carries inherent financial risk. Venture capital firms analyze that risk and then manage it by adjusting their financial expectations—the higher the risk, the higher the expected financial returns. And the financial risk is considerable: In traditional venture capital operations, few investments meet or exceed projected returns.

For community development venture capital investments, financial expectations are more modest. (See the box, “Evaluating CDVC Investment Success.”) “The traditional venture capital firm is searching for home runs. We expect to have fewer home runs, but more doubles and singles,” states Coastal Ventures’ Henshaw. And CDVC firms manage that risk somewhat differently, providing strong technical and management assistance to the entrepreneur.

CDVC carries another dimension of risk—community development risk. According to Meriwether Jones, this dimension of risk requires measurement and management, just like financial risk. Community development risk is measured by the broader social and economic implications of a firm’s success or failure. For example, if a candidate for an equity investment proposes to hire a large number of low-income people, the firm runs the risk of not finding enough appropriately qualified people. If the firm is not able to fill needed positions, it could mean failure for the business; it could also mean continued unemployment for residents and continued economic instability for the neighborhood. With such a risk identified, a fund might manage it by linking a firm with an employment training organization in the community.

A Relationship Industry

Because CDVC professionals recognize the importance of managing both financial and community development risk, they define their relationships with entrepreneurs more broadly than traditional equity investors.

At BCLF Ventures, Hakim Dyer establishes relationships with the entrepreneur long before an enterprise is ever funded, working with the firm to develop a business plan, to perform market research, and to conceive a marketing strategy. By doing so, he gains a full understanding of the opportunities of

Once an enterprise is funded, CDVC practitioners consider their ownership a means to deliver technical assistance and to encourage socially beneficial products and practices. Because he is involved so early in the firm’s funding process, Hakim Dyer looks at this role as a natural outgrowth of his relationship with an entrepreneur. He reports that, along the way, he assists with marketing plans, advises on management issues, and helps entrepreneurs balance financial and social expectations.

Bridging Gaps

Community development venture capitalists are always looking to help establish entrepreneurs as full participants in the larger economy. To do so, they must bridge the gap between marginalized urban and rural low-income communities and the larger economy.

Once an enterprise is funded, the broader goals of community development venture capital mean different financial expectations:

1. Community development equity investments are often a fraction of venture capital investments, which commonly start at one million dollars.
2. The life of the investment is substantially longer, with exit not expected for five to seven years.
3. Investments are illiquid for longer periods, providing time to focus on the mission of creating quality jobs for low-income people.
4. CDVC investments will not make as much money. Expectations range from 10 percent to 15 percent over an entire portfolio, depending on the emphasis placed on social versus financial returns.
5. Investor stock acquired through CDVC investments is generally sold through a management stock repurchase or an employee stock ownership plan.

Evaluating CDVC Investment Success

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Sources of Capital

Prospects for attracting investment capital will become clearer as community development venture funds establish track records. Today, sources of investment capital range from individual investors to religious organizations. But banks are the most immediate source for investment

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capital and have shown considerable interest. Bank investments in CDVC funds are eligible for consideration under the new CRA regulation. (See box, page 5, for a discussion of CRA eligibility.) Beyond simple compliance, many banks consider such investments as a way to augment their lending activities; they also see them as a way to revitalize communities, create new customers, and turn a profit. Key Bank of Maine was a first-tier investor in the Coastal Ventures fund. Michael Finnegan, Vice President and Community Development Finance Officer, sees his bank’s investment in economic development terms. “Maine is an undercapitalized state. We see this investment as a way to improve business capitalization in Maine.”

The Formative Stage
The industry is working hard to define and establish itself, and its growth signifies its progress. Organized in 1995, the Community Development Venture Capital Alliance now has 45 member organizations from across the nation. Nick Smith reports that membership grew 150 percent from 1996 through April of 1997; he also receives fifteen to twenty inquiries each month from other organizations interested in establishing their own funds.

The Community Development Venture Capital Alliance works both to develop the discipline and to build capacity and expertise among venture funds. At their annual meetings, speakers discuss such wide-ranging topics as achieving and measuring social impacts and approaches to entrepreneurial assistance. Participants can also receive training in the discipline.

According to Smith, however, the jury is still out as to what impact community development venture capital will have on communities. He names talent and money as the most important factors. In Smith’s vision, business school graduates are the greatest potential resource for talent. “They’re a key future base for the industry,” he says.

Interest from such academic institutions as Harvard Business School may also act as a catalyst for the growth and increased credibility of the discipline. Associate Professor J. Gregory Dees has developed courses such as “Profits, Markets, and Values,” which addresses the role of business in society, and “Entrepreneurship in the Social Sector,” which covers innovative efforts to deliver social goods or solve social problems.

As community development venture capital’s profile rises on numerous fronts – academic, financial, and community development – so will its prospects for attracting talented practitioners as well as private investment capital. But results – whether social, economic, or financial – will determine the ultimate viability of CDVC as a tool in economic development.

For further reading....

To order any of the following papers, contact Becky Carter at the Federal Reserve Bank of Boston. Phone: 617-973-3813; e-mail: rebecca.carter@bos.frb.org.

The Blue Dot: Community Development Venture Capital. Patience and Other Oxymorons, unpublished manuscript by E.B. Tasch.

Ensuring that the “Blue Dot” Ends up Blue, Meriwether Jones, The Aspen Institute, Rural Economic Policy Program, unpublished manuscript.

The Economics of the Private Equity Market, George W. Fenn and Nellie Liang, Board of Governors of the Federal Reserve, and Stephen Prowse, Federal Reserve Bank of Dallas.


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world wide web: http://www.bsr.org

A meeting of CDVC professionals....
Community Development Venture Capital Alliance, meeting and seminar, December 2-4 in Baltimore, Maryland. This meeting will be preceded by a half-day training, Basic Introduction to the Community Development Venture Capital. For more information and to register, call Judy Burton at 218-722-0861.
Many community development venture capital investments qualify for consideration under the new CRA regulation. This is a synopsis of the criteria that guide compliance examiners in considering qualified investments.

Qualified investments include grants to, and investments, deposits, or shares in financial intermediaries, including Community Development Financial Institutions (CDFIs), that primarily serve low- and moderate-income areas or individuals in order to promote community development. An investment in a community development venture fund qualifies if the fund invests in activities that promote community development.

**For Large Institutions**

CDVC investments will be considered under the investment test. The examiner reviews the bank’s investments and, at the institution’s option, those of its affiliates. She also considers qualified investments made since the previous examination and possibly those still outstanding that were made before then.

**Investment Evaluation Criteria**

- The investments must benefit the institution’s assessment area(s) or a broader statewide or regional area that includes the institution’s assessment area(s).
- Whether the investments have been considered under the lending or service tests.
- Whether an affiliate’s investments have been claimed by another institution.
- The dollar volume of investments in relation to the institution’s capacity and constraints and the assessment area’s characteristics and needs.
- The use of innovative or complex investments, particularly those not routinely provided by others.
- The degree to which an investment serves low- and moderate-income areas or individuals.

**For Small Institutions**

A small bank’s “streamlined” exam focuses on lending. An examiner may also consider qualified investments when considering enhancing a “Satisfactory” rating and when reviewing a bank’s loan-to-deposit ratio.

**Enhancing a “Satisfactory” Rating**

An institution may ask an examiner to evaluate its performance in making qualified investments — including those in community development venture funds — that enhance credit availability in its assessment area(s). The examiner may then use that evaluation to enhance an institution’s “Satisfactory” rating.

**The Loan-to-Deposit Ratio**

Investments in community development venture funds may be evaluated as the examiner reviews the loan-to-deposit ratio. If the ratio does not appear reasonable in light of the performance context, the examiner will consider the innovativeness or complexity of qualified investments or of community development loans. These factors will be used to assess how these activities compensate for a low loan-to-deposit ratio or supplement the institution’s lending performance.

**For Wholesale and Limited-Purpose Institutions**

Performance is evaluated using the community development test. This test evaluates the number and amount of community development loans, qualified investments, and community development services.

The examiner considers the institution’s capacity and constraints and reviews the institution’s performance, considering:

- The extent of community development activities.
- The degree of innovation in these activities (for example, by serving low- or moderate-income individuals in new ways). A community development venture fund investment could qualify as an innovative activity.
- The complexity of the institution’s activities.
- The responsive of the institution to opportunities for community development.
- The degree to which the institution’s investments serve needs not routinely provided by other private investors.

**Where Social and Financial Goals Meet**

In June 1996, BCLF Ventures closed its first equity deal — a $50,000 investment in Boston’s WorkSource Staffing Partnership. A temporary services and placement company, WorkSource helps recipients of public assistance make the transition from unemployment to good jobs.

Aiming to develop a business based on the premise that people on public assistance constitute a large and untapped market, WorkSource meets the criteria that many CDVC practitioners seek. WorkSource is looking to capitalize on the needs of private industry while serving the needs of individuals coming off public assistance. Large employers often have difficulty attracting and keeping skilled entry-level employees, while welfare reform requires recipients of public assistance to seek employment. WorkSource is committed to the social aspect of its mission: Wages start at eight dollars an hour; workers also receive health insurance benefits, consult with WorkSource staff on work issues and career planning, and work for firms dedicated to developing and promoting their employees.
In today’s economy, the WorkSource concept makes sense. Employers need good workers, and some are willing to pay for a service to help find and keep them. For its part, WorkSource selects skilled and motivated candidates. The key to success, however, seems to lie in WorkSource’s support and follow-up. This is where the expertise of co-founders Mary Culhane and Neil Silverston comes in. A former social worker, Mary Culhane works closely with each individual: she screens applicants, helps employees make the transition into the work force, meets with each employee weekly, checks in with supervisors, and counsels employees about career development. Neil Silverston (one of the co-founders of City Year, a nationally recognized youth service organization) devotes his time to the business side.

WorkSource Staffing Partnership fills the gap between what employers supply — a good working environment, fair wages, and opportunity for career development — and the “soft” needs of those who have not established a work history. “We help them develop the tools to become professional,” says Culhane. That gap defines WorkSource’s market opportunity. Not set up to deliver “soft” services, client firms look to WorkSource to supply them. And employers are willing to pay for this expertise. WorkSource charges each client firm for its costs — which vary, depending on the service supplied — plus a margin.

Mary Culhane and Neil Silverston have come up with a good recipe for pursuing a financial mission by fulfilling a social mission, which is just what BCLF Ventures is looking to promote. The firm’s success will ride on the market’s continued need for skilled entry-level workers and the quality and consistency of the service they supply to both employees and employers.

New England’s Enterprise Communities: An Experiment in Economic Revitalization

by Susan Cournoyer, Federal Reserve Bank of Boston

With so many fiscal and economic challenges facing them today, stakeholders in local communities often are not sure whether their efforts can make a difference. Yet eight communities in New England, with the support of the federal government, are taking the initiative in collaborative efforts to revitalize their economies. Lessons from these enterprise communities can be useful for all nonprofit organizations, financial institutions, and economic development agencies seeking strategies to create jobs and businesses in economically distressed communities.

In 1993, the Clinton Administration announced the Empowerment Zone and Enterprise Community (EZ/EC) Program as the centerpiece of its urban and rural revitalization strategies. Through late 1994, the federal government oversaw a competitive application process for cities wanting to participate in the EZ/EC program. Applicant cities were required to engage in a strategic planning process involving community residents and a range of community stakeholders. In December 1994, the federal government designated 105 cities — including eight in New England — as enterprise communities or empowerment zones based on the written strategic plans submitted by each applicant city. Along with the designations came $3 million for each of seven

Selected Enterprise Community Initiatives

Manchester, NH
- Revolving loan fund for housing
- Business incubator managed by New Hampshire College

Lowell, MA
- Business information center
- Skills inventory of residents

Boston, MA
- Harry Miller industrial cloth facility
- Job training for 500 residents

Springfield, MA
- Resident computer training
- Training incentive for Cross Country Group Call Center

Providence, RI
- Artisan entrepreneurship program
- Job placement by South Providence Development Corporation

Burlington, VT
- Microenterprise network
- Green manufacturing

New Haven, CT
- Retail/franchise initiative
- Training partnership with local manufacturers
enterprise communities in New England and $25 million for Boston’s enhanced enterprise community, as well as access to tax credit and development financing tools for all of the ECs.

The program establishes a framework of four key principles: economic opportunity, sustainable community development, community-based partnerships, and a strategic vision for change. Each applicant city was required to create its own development and implementation plan based on these principles. For example, in one New England enterprise community – New Haven, Connecticut – financial institutions, government agencies, private companies, and local educational institutions including Yale University now plan to make coordinated investments of over $15 million in New Haven’s low- to moderate-income neighborhoods over the next two to three years. Three million dollars of this investment comes from the federal government, in turn leveraging an additional $12 million of public and private investment in small business financing, job training, and supportive neighborhood development programs.

Community Involvement
Community participation distinguishes the EZ/EC program from federal programs of past eras. Locally established community advisory boards set each EC’s goals and priorities. In fact, EC applications were judged not only by the level of need identified in the community, but also by the strength of the proposed community and economic development partnerships. As President Clinton noted in a recent press conference about enterprise communities, “Instead of big solutions imposed by Washington, it creates a partnership between government, business, and private citizens to help communities lift themselves up.” However, this opportunity also carries some risk that these partnerships could become unwieldy and ineffective in administering the grants. Yet the underlying opportunity may outweigh the risk, for the federal government is wagering that some community partnerships will not only survive, but also – through community initiative – will maintain momentum long after their monies are spent.

Early Challenges
Among the first challenges addressed was the need to establish an effective mechanism for making and carrying out decisions, and so each EC had to transform its advisory board into a coherent governing structure. In Lowell, Massachusetts, for example, the EC engaged outside consultants to facilitate a “Board Retreat,” which familiarized Board members with each other and helped them define their roles and responsibilities.

Although every EC has a Coordinator and an advisory board Chair, beyond these roles the arrangements differ. In Boston and Springfield, Massachusetts, the Mayor appointed each member of the advisory board. In Lowell, the EC held neighborhood elections. Each board includes representatives from the community as well as from nonprofit, private, and government organizations.

A New Federal Role
The EZ/EC program has also meant a new role for the U.S. Department of Housing and Urban Development (HUD), which now supports local efforts rather than directing them as it had in years past. HUD anticipated that the enterprise communities would face challenges, and it has employed enterprise community coordinators to help communities work within the legislation’s framework. Early in the process Paul Horn, the New England Coordinator, helped ECs work toward fulfilling the vision of the EZ/EC legislation. He encouraged the ECs to see each other as resources. And he linked the ECs with consultants to tackle specific projects. For instance, the EC in Manchester, New Hampshire, worked in conjunction with a consultant to seek neighborhood input for a neighborhood community center, resulting in an updated plan for several social service agencies to share a facility in the heart of the community.

“Finding leadership to promote collaboration in enterprise communities can be difficult. Keeping EC ideas in view over time will be a real challenge.”

Paul Horn, EZ/EC Coordinator

Partners and Programs
Communities then started making program funding decisions and established benchmarks to gauge their results. In Manchester, the community advisory board plans to disburse the EC grant among a limited number of programs, including a business incubator, a summer school enrichment program, and an extensive community policing program. The EC in Burlington, Vermont, by contrast, is working with over sixty partnering organizations to fund small-scale, local development initiatives such as a home health care cooperative and a community computer center. Providence, Rhode Island, is banking on one large initiative and a host of nine smaller ones. The South Providence Development Corporation, the largest initiative, links residents to employment opportunities at local hospitals, while smaller initiatives include a microenterprise loan fund and an artisan entrepreneurship program. Boston, by contrast, is spending $3 million on job training and $22 million on loans to small- and medium-sized businesses.

Partnerships in each EC reflect local institutional and economic
strengths. In New Haven, People’s Bank has made $5 million of small business financing available; participation by the EC and two other organizations will add another $500,000 for small business loans. Burlington has focused on microenterprise development, a prominent feature of Vermont’s economy. In Springfield, the EC has worked with the Massachusetts Development Finance Agency to provide an incentive for the Cross Country Group, a call center business, to locate a major facility in the city. And the South Providence Development Corporation intends to place over 250 individuals in health care positions, in partnership with the dense cluster of health care providers in Providence.

Maintaining Momentum
The most critical stage of the EC process may still lie ahead. Sustainability will be the key to ultimate success. After fully committing the federal money, communities will need to gather the financial and institutional support needed to sustain promising EC programs. Less successful programs may need to be phased out, while programs viewed as effective will face the challenge of garnering continued investment. Some communities may be able to maintain the governance infrastructure of their enterprise communities, allowing existing leaders and partners to promote continued collaboration and investment. However, the governance structures in other communities may not persist after the enterprise community money runs out. Notes Paul Horn, “Finding leadership to promote collaboration in enterprise communities can be difficult. Keeping EC ideas in view over time will be a real challenge.”

Several ECs are already addressing the sustainability question by identifying the long-term interests of partners and communities. Miguel Rivas, working in the Springfield EC, relates the story of two local organizations: “A lot of these organizations used to go off on their own to get funding. Now, for the first time ever they are working together on proposals.” He described a joint proposal by three organizations working in the Mason Square neighborhood of Springfield. By collaborating on the proposal, the organizations obtained more financing for the neighborhood than they could have obtained separately. Similarly, locally owned financial institutions in Lowell see their future linked to Lowell’s growing immigrant community, and they seek to institutionalize this link through joint participation in the EC’s Business Information Center.

Lessons for Other Communities
Two lessons stand out from the EC experience. Perhaps foremost, notes Paul Horn, is that the EC program “encourages communities to try to integrate their thinking.” And by integrating their thinking, ECs can encourage joint planning among nonprofits, initiate conversations between community based organizations, government, and private sector organizations, and link downtown and government representatives with representatives selected by the community.

The second lesson lies in the increased value placed on community leadership in the EC communities. In those ECs where stakeholders set aside past tendencies to try to tackle problems alone, economic momentum can gather through collaborative efforts. From the employment initiatives in Providence to small business incubation in Manchester to microenterprise development in Burlington, collaboration brings results. And that’s a lesson that all communities, financial institutions, and nonprofit organizations can adopt as a best practice, by taking the initiative into local hands to promote economic stability and growth.
Are you the CRA officer of a large financial institution? The following are practical questions raised by five banks and responses from Paul Dillard, Senior Compliance Examiner at the San Francisco Federal Reserve Bank. The questions are organized around the subjects of the former twelve assessment factors, and the replies show how they translate to the new examination procedures.

**Assessingors’ Needs**

**Assessment Factor 1:** brochures, pamphlets, records of meetings, etc., used to ascertain community credit needs.

Is this information useful as part of the new CRA exam procedures? How? Examiners will no longer evaluate a financial institution on ascertainment efforts. However, it is still sound business to identify lending opportunities and loan product needs. This information may be especially useful to examiners as they evaluate the bank’s performance context.

How might this information contribute to the performance context? The exam procedures require examiners to conduct their own performance context evaluation. Examiners will establish contacts with community members for a better understanding of lending opportunities. An examiner will have limited time to conduct these meetings; the more information a bank can supply, the more accurate his or her conclusions will be.

What are the components of a complete performance context? 1) The economic and demographic characteristics of the assessment area(s); 2) lending, investment, and service opportunities; 3) the institution’s product offerings and business strategy; 4) the institution’s capacity and constraints; 5) the prior performance of the institution and, in some cases, the performance of similarly situated institutions; and 6) any other relevant information.

**Assessment Factor 3:** CRA statement, other CRA-related publications, and minutes of CRA meetings.

Is it still worthwhile for the board of directors to oversee CRA policy? Though no longer required, it is still good business to involve directors in any integral function of the institution. It is also good business to involve directors in setting and overseeing CRA activities.

Is the CRA statement still a useful document? If an institution has maintained a very cursory statement, its continued value is questionable. If the bank has an expanded statement, it could be used as a marketing tool. However, a CRA statement does not supersede the requirement of a CRA notice.

**Marketing Data and Credit Offered and Extended**

**Assessment Factor 2:** sample marketing and advertising materials and information on special loan programs.

Will an examiner review this information? Although an examiner will not ask to see marketing materials or sample advertisements, the information regarding special loan programs will be useful as examiners consider the institution’s flexibility and/or innovation under the lending test. Such information could also be helpful in extreme situations, for example, when a bank needs to refute allegations of redlining.

**Assessment Factor 9:** HMDA data, marketing research and information documenting loans to nonprofit organizations.

How should this information be reported under the new procedures? Institutions will continue to report HMDA data in the same manner as in the past. Examiners will use this information to evaluate the following factors: 1) geographic distribution of loans by income level; 2) geographic distribution of loans by borrower characteristics; 3) responsiveness to credit needs; 4) innovative or flexible lending practices; and 5) community development lending activities.

How strict are deadlines on community development and small business/farm reporting? The deadlines are as strict as those for HMDA reporting. The data will be used as part of the bank’s disclosure statement for its Public File. The examiner will also combine it with data from other financial institutions in establishing the performance context.

Will the examiner want to see organizational background information about a bank’s participation in a consortium? Organizational background is useful, particularly if an institution's
employee performs a technical function for the consortium, which could augment the bank’s performance under the service test.

Can financial institutions receive “double credit” for consortium lending? Double credit may be granted in several ways: 1) if a financial institution’s commitment produces loans for the development of low-and moderate-income multifamily housing, the institution may count its pro rata share of these loans under both the mortgage and the community development lending aspects of the lending test; 2) should an institution make a loan pool commitment and an equity investment, it would receive consideration under the lending test as well as under the investment test, based on the size of each commitment; 3) if it invests in a community development bank, the investing institution could choose to have its investment considered solely under the investment test, or it could request consideration under both the lending and investment tests.

**Assessment Factor 10: FHA, SBA, and other government program information.**

Will the examiner want to know if we participate in government programs and, if so, what information will the examiner find useful? This information will be useful to the extent that the program allows the bank to offer flexible or innovative credit terms.

**Geographic Distribution of Loans and Record of Opening and Closing Offices**

**Assessment Factor 5: maps, census tract lists, and data about credit applications, approvals, and denials.**

What methods of documenting geographic distribution of loans are recommended? How far back should data be collected? A variety of software programs will prepare a geographic analysis. Examiners will also conduct a geographic analysis based on either census tracts or block number areas. Their analysis will be based on loan data collected since January 1, 1996.

**Assessment Factor 7: information about branch openings and closings, and services provided.**

The new regulation stipulates that this information be included in the public file; does it also need to be documented anywhere else? Examiners will consider branch openings and closings and the services provided as part of the performance criteria under the service test.

Is it important for a bank’s CRA officer to have input on branch openings/closings? Usually, a financial institution’s directorate, senior management, and branch administration decide on branch openings and closings. However, such decisions sometimes have an impact on low- and moderate-income neighborhoods. Since a regulator will consider such impact in any branch opening or closing application, management should seek input from the CRA officer.

**Discrimination and Other Illegal Practices**

**Assessment Factors 4 and 6: fair lending information.**

What methods will the examiner use to assess fair lending activities? There is no fair lending evaluation under the new CRA, except that the financial institution’s assessment area cannot arbitrarily exclude low- or moderate-income geographies and may not reflect illegal discrimination. If during a bank’s fair lending examination, an examiner identifies substantive issues, the institution may expect a reduction in its CRA rating.

**What information related to assessment factors 4 and 6 should be contained in the new CRA files? Where? These evaluations are now part of**
a fair lending examination. However, information that could explain, for example, lack of penetration in a given geography could head off a potential examiner allegation of redlining.

Community Development Assessment Factor 8: outreach information, volunteer activities, and community development investment information.

How should these activities be divided among lending, service, and investment; what information is needed for each? Community development investment information should be categorized under the investment test unless the bank can provide lending test information (as described under Assessment Factor 9) for consideration under both the lending and the investment tests. Qualified volunteer activities may be counted under the community development services portion of the service test.

How do you recommend we measure service test activity? Community development services must relate to the provision of financial services. Refer to the complete list of qualified community development services in the preamble of the CRA regulation. Measurement is based on the performance context. Analyze the institution's capacity and opportunity to provide them. In cataloging these services, we recommend polling the Board of Directors and senior management. If the record of community development services is still insufficient, the bank could then poll managers at the next level.

How can an institution determine if its levels of lending, service, and investment are “adequate?” Performance context and self-analysis are key. Whether consciously or not, institutions maintain and update their understanding of their performance context. During the course of business, financial institutions commonly gather information on each other, the demographics of their service area(s), and opportunities for lending and investment. All of this information helps establish the performance context. Armed with this understanding, an institution may then conduct a self analysis, which will be based on the bank's own tracking of its lending, investments, and services. This analysis will give the institution a better understanding of its performance.

Assessment Factor 11: information about the bank's financial condition and size.

Is there consideration given for a large institution's size, legal impediments, and financial condition? Yes. This is part of the performance context evaluation.

What information should be provided? Examiners review the financial institution's consolidated report of condition, any outstanding supervisory actions, and reports by regulators that help examiners to identify peer institutions. If bank management is aware of some limitation that affects the institution, it should share that information with examiners.

Assessment Factor 12: all the data that didn't quite fit the other files, particularly about outreach, community needs, and potential new projects and partners.

What consideration will be granted for withdrawn credit proposals that consumed significant time and resources and, if any consideration is given, where will it appear? Consideration will be granted under the service test to financial institutions initiating such a credit proposal as creation of a CDC only to have the proposal unravel. A bank should have invested at least two months and ample staff time before it can expect to receive credit.
Community Development Venture Capital Alliance, meeting and seminar, December 2-4 in Baltimore, Maryland. This meeting will be preceded by a half-day training, Basic Introduction to the Community Development Venture Capital. For more information and to register, call Judy Burton at 218/722-0861.

National Association of Community Development Loan Funds, Annual Training Conference, November 12-15 at the Radisson Hotel, Burlington, Vermont. Contact Daphne Smith at 215/923-4754.


National Association of Affordable Housing Lenders, Regional Conference, September 4-5 at the Sheraton Boston Hotel & Towers. For registration information, contact Thea Bicbering, by phone at 202/861-5770, by e-mail at info@naahl.org.

Operations Guide for Community Development Loan Funds. From the National Association of Community Development Loan Funds. Each chapter includes basic principles, details, and examples of community development loan fund operations. Contact Daphne Smith at NACDLF at 215/923-4754.

Community Reinvestment Act Interagency Questions and Answers, issued by the Federal Financial Institutions Examination Council. This Q&A answers many questions raised about the new regulation. To request, contact Becky Carter, Federal Reserve Bank of Boston, 617/973-3813; by e-mail: rebecca.carter@bos.frb.org.

Community Reinvestment Act Regulations, Joint Final Rule. Revisions provide guidance on the new regulation. To request, contact Becky Carter, Federal Reserve Bank of Boston, 617/973-3813; by e-mail: rebecca.carter@bos.frb.org.

Examination Procedures for the New Community Reinvestment Act Regulation. Procedures outline guidelines for compliance examiners to follow when conducting a CRA examination. To request, contact Becky Carter, Federal Reserve Bank of Boston, 617/973-3813; by e-mail: rebecca.carter@bos.frb.org.

Partners. This computer software program is an analytic tool for financial institutions, community groups, and other community development professionals to use in counseling low- and moderate-income applicants. From the Federal Reserve Bank of Boston. To order free of charge, call 617/973-3459.