Community Reinvestment Act (CRA) Motivated Capital

TL;DR

The Community Reinvestment Act (CRA) requires regulated financial institutions to help meet the credit needs of all communities in the service area they are chartered to operate. In turn, financial institutions often invest in intermediaries (such as CDFIs) serving low- and moderate-income communities and can be a promising potential capital source for innovative funds.

How does the CRA work?

The Community Reinvestment Act was enacted in 1977 to help verify that federally insured banks meet the credit needs of the communities in which they are located, consistent with safe and sound banking practices. The CRA was one of several laws passed during the 1960s and 1970s to expand access to credit in response to the federally endorsed practice of "redlining" and other institutions of systematic discrimination.

Three federal regulators—the Office of the Comptroller of the Currency (OCC), the Federal Deposit Insurance Corporation (FDIC), and the Federal Reserve Board—share oversight of the CRA. Neither the CRA nor its implementing regulations prescribe ratios or benchmarks that regulators must use in the evaluation or application processes. Instead, the CRA encourages banks to help rebuild and revitalize communities through sound lending and good business judgment that benefit both banks and the communities they serve.

The CRA provides a framework for depository institutions and community organizations to work together to promote the availability of credit and other banking services in low- and moderate-income communities and for low- and moderate-income individuals. Besides directly funding credit-challenged communities, banks can also satisfy their CRA obligations by funding third-party financial institutions, often including (but not limited to) CDFI loan funds, CDVC funds, state and local governments, community development organizations, and even private, impact-oriented investment funds.

On May 5, 2022, 45 years after its creation, the three federal agencies tasked with managing the CRA announced a plan to strengthen and modernize the Community Reinvestment Act. Forthcoming changes to the CRA likely include several key elements, which should improve the outlook for nontraditional capital providers seeking to capitalize funds with CRA-motivated bank partners.

How can capital providers prepare to raise capital from CRA-motivated financial institutions?

1. Focus on elements of your fund or capital product(s) that are:
    - Innovative
    - Complex
    - Responsive

2. Identify FDIC, OCC, and Federal Reserve geographic areas relevant to your efforts on the FDIC website.

3. For OCC-regulated banks, CRA compliant investments must be "Public Welfare Investments," i.e., investments that have an impact on low-moderate income geographies or demographic groups.

4. Sign up for newsletters from local OCC, FDIC, and Federal Reserve offices to keep an eye on trends in local CRA capital markets.

5. Sometimes a bank's CRA department is housed under compliance—there isn't always a dedicated CRA department or manager.

6. Fund managers should consider pitching their funds as nonconcessionary to banks' CRA officers or CFOs. Woodforest Bank, for example, saw Blueprint Local Opportunity Zone Fund as an investment to not only achieve CRA-qualified impact outcomes but also achieve competitive returns.

7. CRA investors are geographically specific. A good way to find local CRA capital is on the FFIEC website, by searching for the geography in which you're located and determining which banks have deposits in your region. Banks are required by law to deploy CRA capital in every area where they receive deposits. As an example, Woodforest had a side letter with Blueprint Local, asking for best efforts to deploy capital within certain geographies where the bank had deposits.

8. Timing is everything when talking to a bank. Their interest has everything to do with where they are in their exam cycle—which ranges from 3 to 5 years. Near the end of the cycle, the team is getting exam ready and focusing on reporting; at earlier stages in the cycle the CRA team might be more willing to invest. Often if the answer is no, this may be a sign to revisit the conversation a year later.

9. Banks are risk-averse. If you're a new fund, focus on the qualifications of your individual team members and your unique track records to compensate for the fund's lack of experience.

10. Prospecting for CRA capital might go better with banks that have recently received a poor compliance rating and, therefore, might be open to investing in a high-impact fund in order to bolster their rating for their next exam cycle.

MINI CASE STUDY

Woodforest National Bank - Blueprint Local Fund Investment

Woodforest National Bank is a privately held, OCC-regulated bank headquartered in The Woodlands, Texas. The bank has nearly 800 branches across 17 states, and readers may recognize Woodforest as Walmart and Sam's Club's largest retail partner. Woodforest National Bank's Community Reinvestment Act (CRA) team is widely recognized as a leading institution among banking and community development practitioners for their innovative approaches to funding impactful and fiscally sound projects in a way that simultaneously satisfies the banks' CRA obligations. One such example of Woodforest's achievements in this arena includes several investments into private investment funds managed by Blueprint Local.

While it is uncommon, banks like Woodforest are able to satisfy their CRA requirements by making a traditional LP (limited partner) investment in an impact-motivated, for-profit investment fund. Blueprint Local, an impact investment fund manager focused on investing in federally designated Opportunity Zones, has received several significant contributions to its regionally focused Qualified Opportunity Funds from Woodforest National Bank. These contributions from Woodforest take the same form as an investment from any other limited partner investor; yet for Woodforest, the nature of the investment funds' commitments to investing exclusively in Opportunity Zones allows these investments to count toward the bank's CRA obligations. In this way, Woodforest not only expands the capacity of a unique private investment fund manager to create greater impact in communities, but also participates in the positive financial returns of this fund, therefore enabling the bank to make further investments of this type in the future.

As a form of risk mitigation, Woodforest requested that Blueprint Local sign an independent contractual agreement, often referred to as a "side-letter," to ensure that, to the best of the fund manager's ability, Woodforest National Bank's capital would be invested exclusively in high-impact projects in low-to-moderate income census tracts (which frequently overlap with Opportunity Zone tracts).