APPENDIX D: Best Practices Research

CRA best practices guide the development of long-term strategies for financial institutions to identify and respond to the credit needs of an assessment area in an effective manner that promotes greater compliance with the CRA. Indeed, "developing a CRA strategy, setting goals, and monitoring results can make CRA performance more predictable and more meaningful."[1] The four best practices for CRA compliance are: (1) Creation of a Performance Context, (2) Goal setting, (3) Tracking of CRA activities, and (4) Monitoring CRA performance.

Create a Performance Context

The first step in carrying out the CRA's best practices is the creation of a Performance Context (PC). A PC lays the foundation for creating an effective CRA strategy that considers the financial institutions particular business advantages and the needs and opportunities within its assessment area.[2] Adherence to this best practice is discussed below in two parts: the purpose of creating a PC, and the methodology for doing so.

1. ***The Performance Context****:* As defined in the Interagency Question and Answers, "[a] performance context can be thought of as evaluating factors external to a bank and internal factors that will influence a bank's performance, how well it meets various community needs, and which community needs the bank chooses as its focus."[3] The CRA does not mandate the creation of a PC by financial institutions, but the government agencies enforcing the CRA strongly encourage a robust PC to be developed to identify the credit needs and potential opportunities for involvement in an assessment area.[4] Other benefits flowing from the creation of a PC include:
    a. *Supports qualitative considerations*. CRA programs that are responsive and innovative begin with the PC through understanding assessment area needs beyond the lens of quantitative data. Furthermore, a financial institution may be required to show examiners how its programs have been responsive and innovative in addressing the credit needs of its assessment area before receiving CRA credit for those programs; a PC provides the context for demonstrating those characteristics.[5]
    b. *Creating the financial institution's "Story."* A financial institutions PC can aide CRA examiners who may have difficulty in identifying the community credit needs and opportunities within a given assessment area. Additionally, the PC's qualitative data allows financial institutions to create a narrative of its assessment area needs and opportunities which are not fully or accurately captured by quantitative data alone.[6]

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[1] Gates, C., & Villanueva, M. Community Reinvestment Act: Developing a Strategy for Success (2014)
[2] Gates, C., & Villanueva, M. Community Reinvestment Act: Developing a Strategy for Success (2014)
[3] National Community Reinvestment Coalition. *CRA Performance Context: Why it is Important for Community Development and How to Improve it* (2015)
[4] A good PC "[is] about strategic and creative thinking at the front end, rather than doing the performance context after the fact and then merely using it to justify what you did and why. . ."
Choi, L., & Dowling, W. *Understanding Community Development Needs through the CRA Performance Context*. (2014)
[5] "A truly responsive and innovative CRA program should begin with the [PC], or knowledge about the bank's local markets. . ."
Choi, L., & Dowling, W. *Understanding Community Development Needs through the CRA Performance Context*. (2014)
Gates, C., & Villanueva, M. Community Reinvestment Act: Developing a Strategy for Success (2014)
[6] ". . . simply compiling easily accessed quantitative data, this approach fails to capture the nuance of the underlying factors that drive that data. As such, examiners rely on interviews with community contacts that can provide details on the local community, such as information on opportunities for banks or perceptions on the local performance of financial institutions."
Choi, L., & Dowling, W. *Understanding Community Development Needs through the CRA Performance Context*. (2014)

Setting Goals

Subsequent to the development of a PC, financial institution's should set reasonable goals for their CRA program. Goal setting provides an effective way for financial institutions to focus on desired outcomes ex-ante.[7] In creating CRA goals, financial institutions should consider the following:

1. *Timing*. Prior to setting goals, the financial institution should discuss and decide on the performance rating it wants to achieve.
2. *Set appropriate goals*. Goals should be measurable, relevant and appropriate to the institution. That is, "aligning the CRA goals with the bank's lines of business and relative market strengths and community credit needs enable an institution's board of directors and management to facilitate and encourage efforts to achieve them."[8]
3. *State the desired impact*. Within each goal, the desired impact can be included. The impact can be stated in terms of numbers or percentages of loans, investments, or services provided or in terms of the number of people that benefited from the activity.[9]
4. *Review past data*. A financial institution should review past performance evaluations and information in public file, including complaints about its CRA performance. It is also helpful to know what similar institutions have done by, and to review for any changes within an assessment area to its demographics, economic conditions, needs and opportunities, and any changes to the institution's internal factors.[10]

Once appropriate goals are set, a financial institution should verify that the goals properly represent the needs of its assessment area. In particular, discussions with community organizations and local government agencies can provide a good check on whether an institution's goals are aligned with the needs of the community.[11] Once verified, an action plan identifying key individuals and groups along with how its goals are to be achieved, and specific timeframes for meeting those goals should be developed.[12]

Tracking

Following the practice of goal setting is the need to implement an effective tracking system that will allow the institution to monitor its CRA performance in light of its goals, including identifying any conspicuous gaps in its CRA activities that may not be readily apparent.[13] A tracking system should enable the creation of useful reports, lists or charts detailing the institution's CRA activity, which allow a CRA officer to analyze and evaluate how effectively an institution is meeting its goals and strategies, in addition to its comparison with prior CRA performances.[14] Examples of useful reports that can be developed from the information collected include:

- Bank-wide or assessment area - specific community development activity reports.
- Community development activity trend reports by year, assessment area or region.
- Community development activities by the organization.
- Quarterly, semi-annual or annual reports detailing the bank community development activities.[15]

Creating an effective tracking system requires adequate training and data collection methodologies.

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[7] Gates, C., & Villanueva, M. Community Reinvestment Act: Developing a Strategy for Success (2014)
[8] Gates, C., & Villanueva, M. Community Reinvestment Act: Developing a Strategy for Success (2014)
[9] Gates, C., & Villanueva, M. Community Reinvestment Act: Developing a Strategy for Success (2014)
[10] Gates, C., & Villanueva, M. Community Reinvestment Act: Developing a Strategy for Success (2014)
[11] Gates, C., & Villanueva, M. Community Reinvestment Act: Developing a Strategy for Success (2014)
[12] Federal Reserve. *CRA Community Development — Examiner Insights*. (2016)
[13] Yarwood, D. *CRA: An Examiner's Perspective Train for Results!* Federal Reserve Bank of St. Louis. (2017)
[14] Berg, T. Strategies for Effective Management of Community Development Activities (2017)
[15] Berg, T. Strategies for Effective Management of Community Development Activities (2017)

1. *Training*. The provision of CRA-aware training provides several important benefits to an institution, including decreasing the probability that CRA-related activities are overlooked and therefore not presented to the examiner and reducing the costs of exam preparation.[16] CRA-aware training can be defined in the following way:

   > "CRA-aware training is a blend of technical requirements, communication of respective assessment area credit and community development needs, identification of geographies and populations driving credit and community development needs, and communication of the institution's CRA strategy for meeting those needs."[17]

   CRA training is ideal for branch managers, lending officers, staff, and other retail banking management.[18] Trainee's do not need to become CRA experts in order to support an effective tracking system, but they should be able to identify possible CRA qualified activities. When applicable to the institution, training on the lending test should include how to identify names of locations within an assessment are that are categorized as low-or moderate-income census tracts.[19] In general, training should be provided before the institution begins tracking CRA related activities since it requires that officers, staff and other employees are capable of identifying which activities may qualify for CRA activities.[20]
2. *Data Collection*. An effective tracking system should continuously collect and organize data on potential CRA activities in a centralized process. If continuous tracking is not feasible, periodical data collection is sufficient. In general, ongoing data collection is meant to protect the institution from retroactively compiling data on CRA activities which threatens the integrity of the data collected.[21] A centralized system that is accessible and easy to use should be utilized for ongoing data collection, such as proprietary intranet systems.[22] Institutions should maintain backup documents - letters, descriptions of projections, populations served, etc., and conduct data integrity reviews since the examiners will be doing the same.[23]

Monitoring

A financial institution that creates appropriate and measurable goals, and that collects CRA related activity data on an ongoing basis, is well positioned to monitor its CRA performance prior to the conclusion of the examination period and to make adjustments as needed. Implementing an effective monitoring system can be viewed in two parts: the need to be informed and to conduct a self-assessment.

1. *Staying Informed:* Monitoring CRA performance necessitates the need to be up to date on community needs and internal changes to the institution, in addition to any guidance and procedure changes for the CRA. To remain informed on community needs an institution can review the recent CRA evaluations of its competitors.[24] Additionally, maintaining relationships

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[16] Yarwood, D. *CRA: An Examiner's Perspective Train for Results!* Federal Reserve Bank of St. Louis. (2017)
[17] Yarwood, D. *CRA: An Examiner's Perspective Train for Results!* Federal Reserve Bank of St. Louis. (2017)
[18] Yarwood, D. *CRA: An Examiner's Perspective Train for Results!* Federal Reserve Bank of St. Louis. (2017)
[19] Yarwood, D. *CRA: An Examiner's Perspective Train for Results!* Federal Reserve Bank of St. Louis. (2017)
[20] Federal Reserve. *CRA Community Development — Examiner Insights*. (2016)
[21] Gates, C., & Villanueva, M. Community Reinvestment Act: Developing a Strategy for Success (2014)
Federal Reserve. *CRA Community Development — Examiner Insights*. (2016)
Yarwood, D. *CRA: An Examiner's Perspective Train for Results!* Federal Reserve Bank of St. Louis. (2017)
[22] Gates, C., & Villanueva, M. Community Reinvestment Act: Developing a Strategy for Success (2014)
[23] Federal Reserve. *CRA Community Development — Examiner Insights*. (2016)
[24] Federal Reserve. *CRA Community Development — Examiner Insights*. (2016)

with government agencies and community groups can help an institution stay up to date on any changes in community needs.[25]

2. *Self-assessment:* By conducting a self-assessment a financial institution is able to make timely decisions about its CRA performance, helping to ensure it maintains a satisfactory rating at a minimum.[26] An effective self-assessment for the monitoring of CRA progress should include a review of lending levels within census tracts of borrow profile and geographic dispersion, if applicable to the performance test.[27] When monitoring progress towards goals it is beneficial to refer to the Interagency CRA Examination Procedures which provides guidance on appropriate proxies for conducting an analysis.[28] If a self-assessment reveals that a bank is failing to meet a goal, it is important to identify the reason for it. The following is a framework for conducting a self-assessment if it is identified that a bank is failing to meet a goal:

    Step 1: Begin by checking the accuracy of the data.

    Step 2: If the data is accurate then consider the following:

    i. Identify any issue(s) or change in the PC that caused the unsatisfactory performance. If the issue or change is temporary then the goals may still be reasonable; but if the change is long-term, the bank should consider adjusting its goals to better reflect the economic realities of its assessment area or its institutional ability to meet the needs of its community. An institution may also look to the performance of similar institutions to confirm if needs and opportunities within the community have changed or if the goals set are unreasonable under the circumstances.

    ii. Identify any changes in the competitive environment, including if activity by new entrants has diluted the previously identified opportunities.

    iii. Identify whether the bank's product offerings are responsive to the needs of borrowers within the assessment area.

[25] Federal Reserve. *CRA Community Development — Examiner Insights*. (2016)
[26] Berg, T. Strategies for Effective Management of Community Development Activities (2017)
[27] Gates, C., & Villanueva, M. Community Reinvestment Act: Developing a Strategy for Success (2014)
[28] Gates, C., & Villanueva, M. Community Reinvestment Act: Developing a Strategy for Success (2014)

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