

STATE OF COLORADO

Department of Regulatory Agencies

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DIVISION OF BANKING

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OPERATING MEMO

TO: Division of Banking Staff

FROM: Barbara M. A. Walker, State Bank Commissioner

DATE: June 9, 1992

RE: Community Development Corporation and Investment Program

BACKGROUND

Under Rules CB101.60 and IB-57, originally issued as ERCB101.60 and ERIB-57, a commercial or industrial bank may make equity and/or debt investments in a community development corporation (CDC) or a community development project (CD project). National banks have had such authority for many years. This Operating Memo provides guidelines for implementation of the Rules.

Bank investments in CDCs or CD projects promote community welfare and simultaneously expand a bank's investment and market opportunities. They generally stimulate, and do not compete with, private sector investment of development companies. National banks have invested in CDCs or CD projects which have:

- Acquired, rehabilitated, constructed, managed, sold, and promoted real estate in their target communities;
- Made equity investments in real estate, commercial projects, and local small businesses through joint ventures, limited partnerships, or other vehicles;
- Provided loans and grants for revitalization activities;
- Mobilized and leveraged a variety of funding resources, both public and private;
- Provided technical assistance in areas such as small business management and home mortgage lending; and
- Conducted community development-related research, such as project feasibility and market studies.

THE COMMUNITY DEVELOPMENT INVESTMENT PROCESS

This section presents the Division's guidelines for commercial and industrial bank CDC and CD project investments.

Structure of Community Development Investments

Commercial and industrial banks can invest in community development initiatives under Rules CB101.60 and IB-57, respectively, in two primary ways: (1) by creating a de novo CDC, either a bank subsidiary, or a multi-bank or multi-investor CDC in which the bank has an ownership position, or (2) by investing in a CDC or CD project over which the bank has not direct control. Both types of investments may be consistent with state statute and rule if they meet the policy guidelines set forth in the Operating Memo.

Community development investments have been structured in a variety of ways including as:

- A wholly or substantially owned subsidiary of a bank;
- A "multi-bank" CDC owned primarily by financial institutions such as a bank, savings and loan association, and/or holding company, provided such CDC complies with applicable state and federal laws;
- A nonbank CDC created and chartered pursuant to specific state, federal, or local statutes;
- A private CDC that was incorporated with express purposes consistent with those described under the "Public Purpose" section of this Operating Memo; and
- A CD project in which the bank makes a debt investment or a CD project in which it takes and equity interest as a limited partner.

Public Purpose

Under Rules CB101.60 and IB-57, a commercial or industrial bank may make debt and equity investments in CDCs and CD projects, subject to certain conditions, provided that they primarily serve a public purpose. Public purpose investments are generally those that:

- Promote housing and economic revitalization or development in low- and moderate-income areas or target areas selected by federal, state, or local government for redevelopment; and
- Directly benefit low- and moderate-income residents of small business.

Although a CDC in which a commercial or industrial bank may invest must primarily promote community welfare, it is not precluded from engaging in entrepreneurial activities in connection with providing public benefits.

Community Involvement

Community involvement in the management and activities of a CDC is a major factor in assuring that the CDC meets the public purpose standard of Rule CB101.60 or IB-57. The board of directors of a CDC in which a commercial or industrial bank invests should include community representatives from the affected business, residential and government sectors. The following three factors are also important considerations in assessing community involvement:

- The previous involvement of the bank with community groups, business organizations, and local government;
- The CDC's other methods of involving community representatives in the decision making process, e.g., neighborhood advisory councils; and
- The role of community groups in the implementation and planning of CDC investments or projects, e.g., joint ventures.

Community involvement is also a key consideration in evaluating the public purpose of a CD project investment. The composition and experience of the board of directors of the sponsoring nonbank organization, documented community and public sector support for the project, and the involvement of community groups in project implementation are important factors.

Commitment of Bank Resources

A further consideration in reviewing commercial or industrial bank CDC or CD project investments is the bank's commitment to providing adequate financing and assuring effective management. When a bank is invested in a de novo CDC, adequate capitalization generally means clear designation of start-up capital, including the initial equity and debt investments. In addition, the plans for permanent funding (equity and lines of credit) over a specified time frame generally are included in any preliminary financial plan.

One way for a commercial or industrial bank to assure adequate management is to designate an executive director with administrative and technical skills appropriate to the type of projects to be undertaken. When the executive director is a bank official, he or she normally allocates at least one-half of his/her time to CDC administration. If a bank invests in a nonbank CDC or in a CD project, the management of the CDC of the CD project should demonstrate the experience and skills needed to accomplish its goals.

Future Value of Investments

Rules CB101.60 and IB-57 state the "banks are asked to contribute to a community development corporation, wherein the bank will receive an equity interest in or evidence of debt which may have value in the future...." In interpreting this provision, the Banking Board will approve the creation of bank CDCs as for-profit corporations under the following conditions:

The CDC shall not pay dividends during the first three years of the CDC's operation; and

- The Banking Board may authorize distribution of dividends after three years only after a determination that the CDC has met the public purpose requirement of Rule CB101.60 or IB-57.

Any dividends authorized by the Banking Board are required to be used by the bank in fulfilling civic, community, or public purposes. Factors that may affect whether the Banking Board authorizes dividends include:

- The CDC's retention of the property after a private market has developed which would provide substantially similar services and facilities for the specific project; and
- The use being made of the profits, if any, in the community being served by the CDC.

The approval of the Banking Board is not required on dividends on CDCs which received OCC approval.

Banking Board Review

The Deputy Bank Commissioner is the primary contact for banks interested in making investments under Rule CB101.60 or IB-57 and this Operating Memo. Information from the bank required to review the investment includes, but is not limited to, the following:

- A draft investment proposal with information regarding how the bank's proposed investment meets the guidelines of this Operating Memo and addresses the requirements of the Rule CB101.60 or IB-57;
- Draft copies of relevant incorporating documents; and
- A request for review of any banking law questions that may be identified (together with a preliminary review by bank counsel). Legal review requests should normally:
 - Identify the specific provisions of banking law, including Banking Board rules, in question.
 - Identify all relevant persons and banks involved. Letters relating to hypothetical situations will not be answered.
 - Provide a concise description of the particular legal problem and all facts necessary to reach a conclusion in the matter.
 - Indicate the bank's counsel's opinion of how the legal issues should be resolved, and the basis for the opinion, including an analysis of any relevant court decisions, statutes, and regulations.

For complete information required for Banking Board review contact the Division of Banking.

Within 60 days of receipt of a completed CDC investment proposal, the Banking Board will send to the bank an opinion letter regarding whether or not the proposed investment described by the bank is consistent with Rule CB101.60 or IB-57 and this Operating Memo. The Banking Board's letter will describe all legal, policy, and other conditions that apply to the approval.

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