Comptroller of the Currency
Administrator of National Banks

Washington, D.C. 20219

December 6, 2004

Francis X. Grady
Grady & Associates
20950 Center Ridge Road, Suite 100
Rocky River, OH 44116-4307

Dear Francis X. Grady:

This is in response to your Freedom of Information Act request dated November 17, 2004, received in my office on November 12, 2004. Your request, 2005-131, has been granted.

You requested: a copy of a letter sent to the OCC in 2004 by an unidentified national bank, in which the bank sought to offer a CRA investment option to other banks. Materials relevant to your request are enclosed with an invoice for charges, if any.

Sincerely yours,

Jacqueline J. England

Jacqueline J. England, (202) 874-4873
Disclosure Services
Communications Division

[redacted]

[redacted]
Vice President & Counsel

April 24, 2003

Margaret Hesse
Community and Consumer Law
Office of the Comptroller of the Currency
250 E Street SW
Washington DC 20219

Re: CRA Qualified Investments and Bank-Owned Life Insurance

Dear Ms. Hesse:

[redacted], a division of [redacted] ("[redacted]") respectfully requests confirmation that the OCC will afford CRA consideration to a qualified investment obtained with a bank's funds that were deposited in a separate account in connection with the purchase of bank-owned life insurance ("BOLI"). The separate account contemplated by this request would be comprised solely of investments intended to be CRA qualified, and each investment would be designated to a specific bank and benefit that bank's assessment area(s) or a broader statewide or regional area that includes its assessment area(s) [redacted] is making this request in contemplation, together with an insurance partner (the "Insurer"), of offering this investment option as one of the investment options inside of BOLI.

BOLI Overview

BOLI is life insurance purchased and owned by a bank to offset the costs of post-retirement employee benefits and to insure against the risk of loss of key officers or employees. The OCC specifically recognizes the authority of national banks to purchase BOLI[1] and provides extensive guidance to help ensure that BOLI purchases are consistent with safe and sound banking practices.[2]

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[1] "The authority for national banks to purchase and hold life insurance is found in 12 USC 24 (Seventh), which provides that national banks may exercise 'all such incidental powers as shall be necessary to carry on the business of banking.' Purchases of life insurance that the OCC has found to be incidental to banking include key-person insurance, insurance on borrowers, insurance purchased in connection with employee compensation and benefit plans..." OCC Bulletin 2000-23 at 1.

[2] OCC Bulletin 2000-23.

[redacted]

A bank may elect to purchase BOLI as a separate account product, in which the premium paid by a bank at the time the policy is purchased is not invested in the general account of a life insurance company but, instead, in a distinct account comprised of premiums from several bank-policyholders. Although the funds paid into the account are from bank-policyholders, state and federal insurance regulation provide that the separate account itself is owned by the insurance company which also controls investment decisions.[3] However, as the OCC notes, "[t]ypically, the policyholder of separate account products assumes all price risk associated with the investments within the separate account."[4]

Separate BOLI Account Devoted to CRA Qualified Investments

The Insurer has proposed offering a separate BOLI account that would be comprised exclusively of investments intended to be qualified under the CRA ("BOLI-CRA Account"). The BOLI-CRA Account would be made available to bank-policyholders that wanted to employ their BOLI premium dollars to advance the goals of the CRA, rather than investing those dollars in other investment options. The Insurer has indicated that for banks which select this account option, it will purchase and hold a distinct investment based on the specific CRA needs of each bank-policyholder, including the Bank.[5] All such investments would then be pooled in the separate account in a mutual fund-like manner, and the return to each bank- policyholder would be based on the overall return of the portfolio.

OCC Supervision of Separate BOLI Accounts

The OCC does not substantively distinguish between investments a bank makes directly and investments held on behalf of a bank in a separate BOLI account. Indeed, the OCC requires a bank to employ fundamentally the same due diligence standards for investments held on the bank's behalf in a separate BOLI account as the bank must employ for investments it makes directly.

The OCC's guidance on BOLI states that the "safe and sound use of bank-owned life insurance depends on effective senior management and board oversight,"[6] and

[3] "In order for a bank to enjoy tax-deferred build-up of the BOLI cash value, the separate accounts must be under the ownership of the insurer and not the bank. The bank can have no control over individual investment decisions." American Bankers Association, "Bank Owned Life Insurance," May 25, 2001.
[4] OCC Bulletin 2000-23 at 12.
[5] For example, the insurer may purchase a Chicago-based qualified investment on behalf of a bank-policyholder with a CRA assessment area of Chicago and a New York City-based qualified investment on behalf of a bank- policyholder with a CRA assessment area of New York. Both investments would be held in the same separate account.
[6] OCC Bulletin 2000-23 at 2.

delineates the numerous responsibilities of a bank and its board throughout the BOLI process. The OCC specifically cautions banks on the interest rate and price risks inherent in separate account BOLI products, particularly in light of the fact that the bank does not control the separate account assets. The OCC twice advises as follows with respect to both risk categories:

> Therefore, before purchasing a separate account product, bank management should thoroughly review and understand the instruments governing the investment policy and management of the separate account. Management should understand the risk inherent within the separate account and ensure that the risk is appropriate for the bank. Also, the bank should establish monitoring and reporting systems that will enable the bank to monitor and respond to price fluctuations.[7]

The OCC reiterated its concern in a 2002 Bulletin stating: "banks purchasing BOLI must demonstrate and document a thorough understanding of the risks associated with this product."[8]

CRA Regulatory Considerations

The CRA regulations and interpretive documents provide substantial support for our position that a bank should receive CRA consideration for an underlying investment held on its behalf in a BOLI-CRA Account, provided that the investment otherwise satisfies CRA criteria. As explained below, neither the pooled nature of a BOLI-CRA Account nor the fact that a third party purchases, owns, and selects the underlying investment contained in that account precludes the OCC from considering the investment to be CRA qualified.

- **The CRA does not require that a bank directly select, purchase, or own a qualified investment in order to receive CRA consideration for that investment.**

The CRA regulations state that the "investment test evaluates a bank's record of helping to meet the credit needs of its assessment area(s) through qualified investments."[9] The test does not require that a qualified investment be selected, bought, or held by a bank, and, in fact, banks routinely receive CRA consideration for qualified investments purchased, owned, and selected by unaffiliated third parties.

[7] *Id.* at 11.
[8] OCC Bulletin 2002-19 at 7.
[9] 12 CFR §25.23 (a).

The Federal Financial Institutions Examination Council interagency CRA Q&As (the "CRA Q&As") unambiguously state that:

> the direct or indirect nature of the qualified investment does not affect whether an institution will receive consideration under the CRA regulations because the regulations do not distinguish between "direct" and "indirect" investments. Thus, an institution's investment in an equity fund that, in turn, invests in projects that, for example, provide affordable housing to low-and moderate-income individuals, would receive consideration as a qualified investment under the CRA regulations, provided the investment benefits one or more of the institution's assessment area(s) or a broader statewide or regional area(s) that includes one or more of the institution's assessment area(s).[10]

Like the equity fund cited in the CRA Q&A above, an investment held in a BOLI-CRA Account would be an indirect qualified investment of the Bank, provided it met the regulatory requirements of having community development as its primary purpose and benefiting a bank's assessment area or a broader statewide or regional area that includes its assessment area.

- **The structure of a BOLI-CRA Account would be analogous to that of other recognized CRA investment vehicles.**

The CRA Q&A quoted above states that a bank will receive CRA consideration for an investment made in an independent fund that, "in turn," makes qualified investments.[11] The BOLI-CRA Account is an analogous instrument. Using bank funds, the insurance company would purchase a CRA qualified investment that benefits the bank's assessment area or a broader statewide or regional area that includes the assessment area.

The BOLI-CRA Account would also clearly meet the CRA's definition of a qualified investment as a "deposit. . . that has as it primary purpose community development."[12] The BOLI-CRA Account would be comprised solely of investments that have community development as their primary purpose, in accordance with the interpretations and directives of the federal bank regulatory agencies.[13]

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[10] CRA Q&As §__.23(a)-1 at 66 Fed. Reg. 36635 (July 12, 2001) (emphasis added).
[11] *Id.* (emphasis supplied).
[12] See 12 C.F.R. §25.12(s).
[13] See CRA Q&As §__.12(h)7 at 66 Fed. Reg. 36625 and §__.12(s) at 36629-30.

- **The pooled nature of a BOLI-CRA account would not be an impediment to receiving CRA consideration for individual investments contained therein.**

For each bank- policyholder that selects the BOLI-CRA Account option, the insurance company would select and purchase an appropriate qualified investment. Like the hypothetical fund discussed in the CRA Q&A above, participants would own an undivided interest in all such underlying investments, and each bank's return would be based on the aggregate performance of all investments in the BOLI-CRA Account.

The OCC and other federal banking agencies (the "Agencies") have expressed opinions that investment vehicles in which ownership interest was undivided but where individual investments were specifically designated to a particular investor may receive favorable consideration under the CRA.

In CRA Interpretive Letter 715 (April 2, 1996), the Agencies deemed the purchase of common stock in a fund of geographically-specific debt securities as "qualified" provided the fund primarily promoted community development. To invest in this fund, institutions would purchase common stock and then designate a "selected target region" in which the fund would invest. Returns to investing institutions would be based on the fund's overall performance, thereby allowing institutions "to make geographically specific commitments and simultaneously receive geographically diverse returns." A BOLI-CRA Account would operate in an analogous manner.

Similarly, in CRA Interpretive Letter 799 (September 3, 1997), the Agencies determined that multiple investors in a fund with commingled assets could receive CRA credit, provided that the underlying investments were "qualified." Letter 799 addressed a private equity limited partnership which, like a BOLI-CRA Account, would have multiple institutional investors who would each have an undivided interest in the fund's assets.

Interpretive Letter 780 (May 5, 1997) considered whether a bank that purchased securities of a trust that invested in state and local bonds throughout the country would "be considered to have invested within its assessment area for purposes of the CRA." The Agencies concluded that securities were "qualified investments," because, as with a BOLI-CRA Account, investments in the trust "will be earmarked for projects located in the institution's assessment area."

Finally, in Interpretive Letter 792 (July 25, 1997), the Agencies found that investors could receive positive consideration under the CRA by purchasing limited partnership interests in a fund which in turn would invest in women-owned businesses. Investors in the fund would designate where the fund was to invest a portion of its assets.

The Letter stated that an institution may receive positive consideration for its entire investment in such an entity, even if the investment is not used by the entity to make qualified investments exclusively in that institution's assessment area.

Conclusion

The OCC should afford CRA consideration to a qualified investment made on behalf of a bank- policyholder and held in a BOLI-CRA Account. Under the current CRA regulatory scheme, a bank may receive consideration for an otherwise qualified investment, notwithstanding that the investment was selected, purchased, and owned by a third party and notwithstanding that the investment is held in a pooled account comprised of individual investments specifically designated to a particular investor.

Moreover, the OCC already treats investments held on behalf of a bank in a separate BOLI account in fundamentally the same manner it treats investments made directly by the bank. Consequently, the OCC should treat CRA qualified investments held in a BOLI-CRA Account in the same manner it treats CRA qualified investments held directly by a bank.

Thank you for your time. If you should have any questions please do not hesitate to contact me at [redacted].

Sincerely

[redacted]

cc: Beth Kirby, OCC
Chris Manthey, OCC