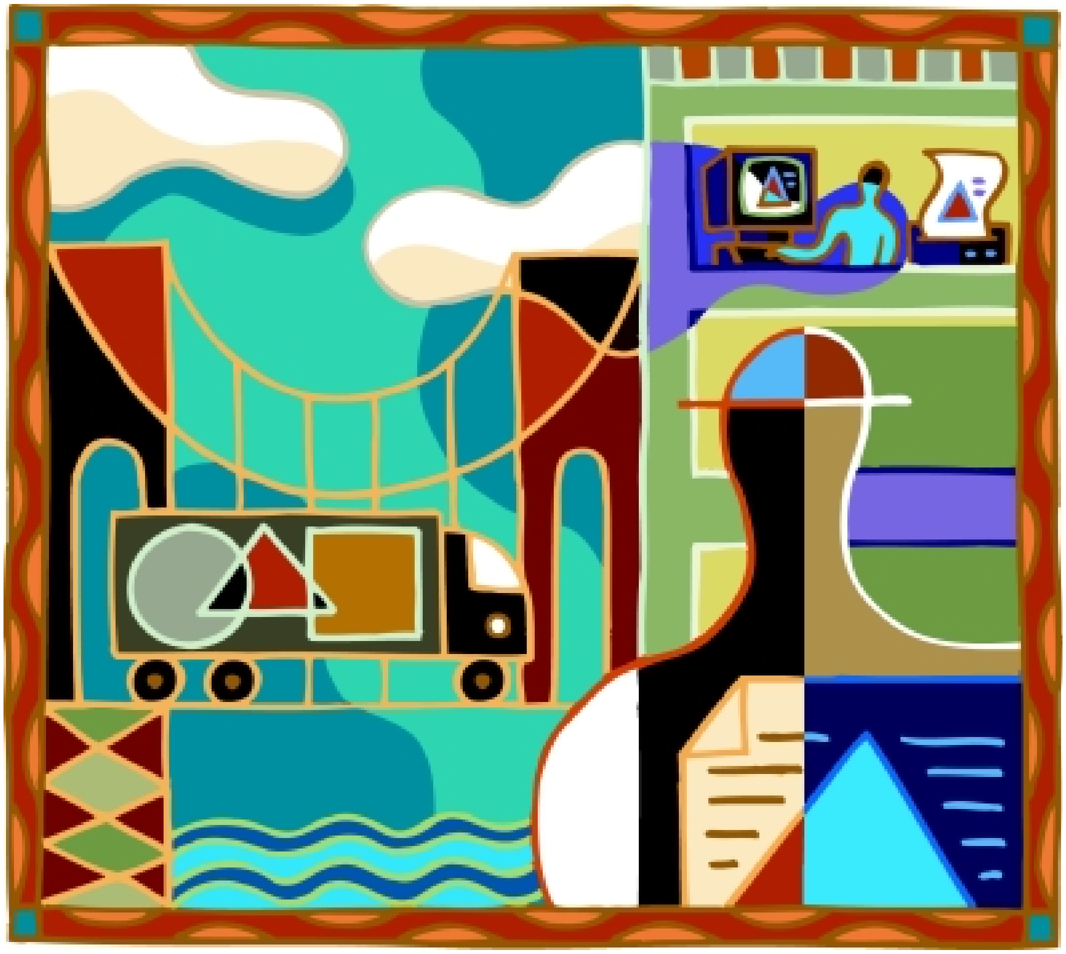
A PUBLICATION OF THE COMMUNITY AFFAIRS UNIT OF THE FEDERAL RESERVE BANK OF SAN FRANCISCO

COMMUNITY INVESTMENTS

A Community • Economic Development Publication

VOLUME ELEVEN NUMBER 3



Credit Scoring for Small Business Lending

We present the results of a 12th District banking survey that examined the use of credit scoring for small business underwriting. Key differences between large and small banks illuminate potential industry trends and raise interesting research possibilities for future study.

Creating Cultural Windows to Banking Opportunities

New immigrant communities across the United States represent tremendous, untapped potential. This article presents some key findings from an ethnic banking study conducted in Los Angeles, and suggests cultural adaptations as a way to reach this underserved market.

Home For Dinner Home Buyers Program

Committed to "finding a way home," a group of Las Vegas financial institutions create an employer-assisted mortgage loan and down payment program for low- and moderate-income employees.

Micropolitan Community Reinvestment Trusts: A CRA Investment Concept for Small Communities

Searching for investment opportunities in small towns can be a CRA officer's worst nightmare. Read on to learn how this CRA investment concept might benefit your financial institution and its assessment area.

Special Insert: More on CRA Investments...

We hope you'll enjoy this edition's special insert featuring excerpts from the 1999 National Conference on Community Development Investments. You'll find solid technical information, and practical tips for today's shrewd CRA investor.

December 99

Community Investments

Editor-in-Chief
Joy Hoffmann Molloy

Managing Editor
Shawn Elliott Marshall

Contributing Editor
Jack Richards

Art Director
Cynthia B. Blake

Production Coordinator
Ariel Andres

If you have an interesting community development program or idea, we would like to consider publishing an article by or about you. Please contact:

Managing Editor
Community Investments
Federal Reserve Bank of San Francisco
101 Market Street, Mail Stop 620
San Francisco, California 94105

Community Affairs Department
www.frbsf.org
(415) 974-2978
fax: (415) 393-1920

Joy Hoffmann Molloy
Assistant Vice President
Community Affairs Officer
Joy.H.Molloy@sf.frb.org

Jack Richards
Community Affairs Manager
Jack.Richards@sf.frb.org

Shawn Elliott Marshall
Community Investment Advisor
Shawn.Marshall@sf.frb.org

H. Fred Mendez
Community Investment Advisor
Fred.Mendez@sf.frb.org

Craig Nolte
Community Investment Advisor
(Seattle Branch)
Craig.Nolte@sf.frb.org

Adria Graham Scott
Community Investment Advisor
(Los Angeles Branch)
Adria.Graham-Scott@sf.frb.org

Lena Robinson
Community Investment Specialist
Lena.Robinson@sf.frb.org

Ariel Andres
Executive Staff Assistant
Ariel.Andres@sf.frb.org

Mary Malone
Protocol Coordinator
Mary.Malone@sf.frb.org

Judith Vaughn
Staff Assistant
Judith.A.Vaughn@sf.frb.org

Editor's NOTEBOOK by Joy Hoffmann Molloy

The last month has seen a flurry of editorial activity and op-ed pieces written about the newly enacted Financial Services Modernization Act of 1999. Clearly, the debate isn't over relative to its potential impact and long-term value. Time and experience will likely serve as the ultimate arbiters.

Debate and conjecture notwithstanding, the Federal Reserve Board is headlong into its own flurry of activity to meet the March 2000 deadline for completion of the legislation's implementing language. We expect this will include the new CRA provisions as well. Although time is short, there are a few proactive steps that financial institutions can take to ensure readiness for implementation of the new law:

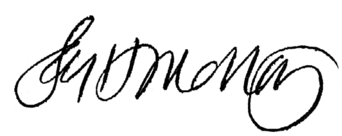
➤ **Develop a mechanism to internally assess and monitor the CRA activities of financial subsidiaries and affiliates**. This is an area where CRA actually got some additional "teeth," since the new law mandates that all financial institution subsidiaries of a bank holding company have at least a satisfactory CRA rating in order to engage in any of the new activities granted under the bill. If even one subsidiary is rated below satisfactory, the expansion application will be denied.

➤ **Review current CRA agreements and create a more formal tracking system for activities within these agreements**. Under the new sunshine requirements, both banks and their non profit partners will be obliged to report (on an annual basis) CRA-related payments, fees, loans, investments, and services and their terms and conditions. Non-profits must also report on the use of said funds, including compensation, administrative expenses, travel, entertainment and consulting/professional fees. Current thresholds mandate reporting of cash payments and grants (individual or aggregate) in excess of $10,000 and loans (individual or aggregate) in excess of $50,000.

➤ **Consider formalizing a CRA self-assessment process and establish close ties with your compliance examiners to make sure you're on the right track.** This will be especially important for small banks with satisfactory or outstanding ratings because they will now be examined for CRA compliance every 4-5 years. (Don't forget that this only applies to CRA, and not other compliance examinations!)

Over the next several months, Congress has charged the financial services industry and its regulators with the task of developing meaningful and workable implementation strategies. We look forward to working with you to achieve this important goal.

Best wishes to you and your family for a wonderful holiday season.



What's Inside

Credit Scoring for Small Business Lending

By Gary Palmer, Banking Studies Officer, Division of Banking Supervision & Regulation, the Federal Reserve Bank of San Francisco

Credit scoring models are increasingly replacing human judgement in lending decisions. Scoring dominates the consumer-lending arena, with the vast majority of credit card and mortgage originations aided by credit scoring models. All indications are that small business lending is going the same route.

During the first half of 1999, the Federal Reserve Bank of San Francisco conducted a survey of 51 12th District financial institutions to learn more about the use of credit scoring in underwriting small business loans. The following presents highlights of the survey results, which cover the extent that scoring is used among large and small banks and the varying approaches to scoring system implementation. The results will also serve as the basis for future Fed research on this topic.

Models for Business Lending

Similar to consumer loan models, small business models use credit history information from credit bureaus to statistically estimate the likelihood that borrowers will repay their loans. For business lending models, credit bureau information for the business' principal owner is used. Additionally, the models factor in information from the loan application such as the business owner's deposit account relationships, liquid assets, and type of business. Sometimes, credit history variables on the small business itself are also incorporated into the models used. This data usually comes from Dunn and Bradstreet.

Typically, the models use some 20–25 variables, and the end-result is a single measure, or score, for each small business. Scores normally range from 300 to 900. The higher the score, the greater a small business's creditworthiness.

Automatic decisioning: Lenders often set policies to allow for automatic lending decisions. Applicants receiving scores above a designated cut-off number are automatically approved, and those receiving scores below another cut-off are rejected. Generally, there's a gray-area in between where human judgement is involved.

In the example below, a lender automatically approves a business loan application when the amount requested is for $50 thousand and less and the business's credit score is 650 and higher. A score between 600 and 649 requires credit officer review, while lower scores result in automatic rejection. This would be the general policy followed by the lender, but with overrides allowed in certain situations.

Lender Survey

To find out more about scoring usage within the 12th Federal Reserve District, a survey was administered informally to a sample of lenders. Completed surveys were returned from the five largest banking companies head-

Example of Decisioning Policy Using Credit Scores

	Credit Score	Action
Loans 50K and Under	650–900	Approve
	650–900	Review ("grey area")
	300–599	Reject
Loans over 50K	600–900	Review
	300–599	Reject

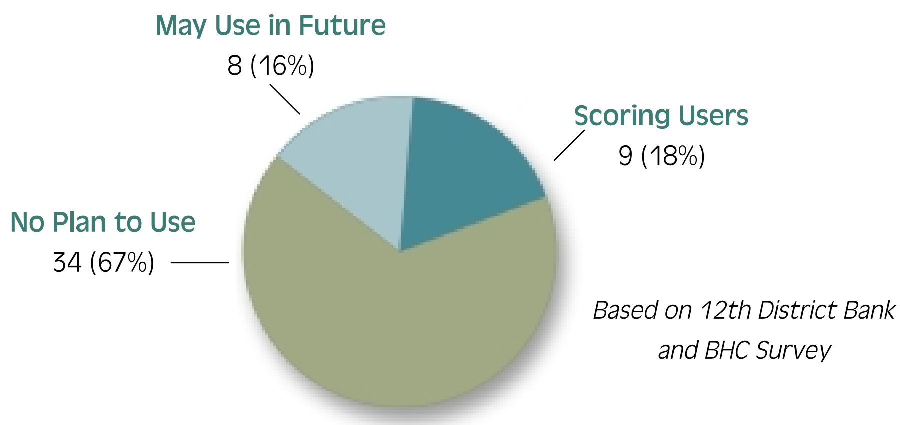
quartered in the District, and from 46 smaller banking companies selected arbitrarily from banks and bank holding companies regulated by the Federal Reserve. They ranged in size from less than $10 million in assets to over $200 billion, with a median size of $195 million.

The survey found that, for these 51 banking institutions, 18% use credit scoring models for business lending, and another 16% are considering using in the future.

While the proportion of banking companies using scoring for business lending is relatively low, a different picture emerges when we look at the lending volume of those organizations. As shown in the chart on the lower left, the nine organizations that use scoring account for over 90% of the small business loans of the institutions surveyed. The five largest District banking organizations all use credit scoring models for business lending: Wells Fargo & Company, Union BanCal Corporation, First Security Corporation, Zions Bancorporation, and BankWest Corporation.

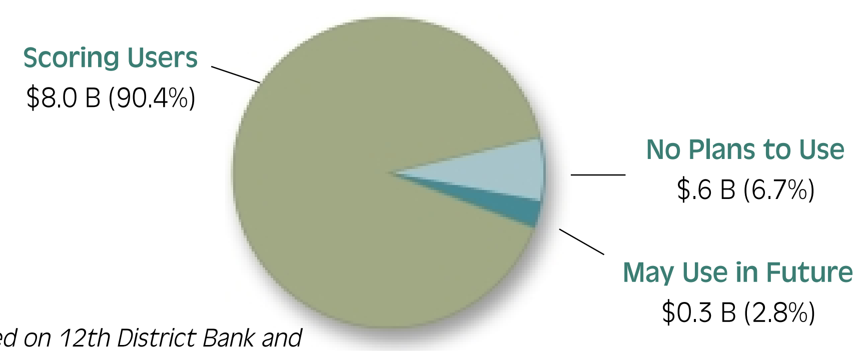
These findings provide support to the notion that small business lending is now dominated by those that use credit scoring models, just as consumer and mortgage lending is similarly dominated by scoring users. Also, given the competitive advantage that is possible, it appears that more and more small and mid-sized banks will adopt scoring over time.

Institutions Using Credit Scoring for Business Lending
Number of Institutions



Based on 12th District Bank and BHC Survey

Institutions Using Credit Scoring for Business Lending
By Small Business Loan Volume



Based on 12th District Bank and BHC Survey – includes loans <$250K only

Survey Questions

Respondents were asked a variety of questions about their credit scoring programs. A summary of their responses follow:

Length of time used: Eight of the nine users implemented their scoring programs within the past three years. Only Wells Fargo started its program earlier. This industry pioneer in credit scoring implemented its small business scoring model in 1989.

Automatic approvals: Six of the nine banks that use scoring automatically grant some loan requests based on customer scores. The other three use scoring to streamline their lending processes, but they continue to subject all loan applications to human review.

Scoring for business expansion: Three use scoring as a means to attract new customers through mail solicitations, but only one uses scoring to expand outside its normal geographic area.

Home-grown or vendor models: Interestingly, all nine of the respondents use scorecards purchased from Fair, Isaac and Company of San Rafael, California. Seven use scorecards from an off-the-shelf Fair Isaac (FICO) model, and two use a customized FICO model. Wells Fargo also uses an internally developed model.

Overall reliance on scoring models: Some of the usage factors and others were combined on the following table to produce a subjective ranking of respondents by their reliance on the models for business lending.

The resulting analytical tool, with the institution names excluded here, considers four factors: 1) the lender use of scoring for automatic loan approvals; 2) the maximum size of loan applications scored; 3) the volume of scored loans on the organization's books; and 4) the use of scoring to facilitate business and geographic expansion.

Extent and Reliance on Credit Reporting

	Institution	Automatic Approvals?	Max Size of Loan Scored[A]	Volume Scored* [B]	Used for Business Expansion?
	Bank A	Yes	High	High	Yes – Geog exansion
	Bank B	Yes	High	Low	No
	Bank C	Yes	Moderate	Moderate	No
Liberal Usage	Bank D	Yes	Low	Moderate	No
	Bank E	Yes	Low	Moderate	Yes – Within existing Mkt.
Conservative Usage	Bank F	Yes	Low	Low	Yes – Within existing Mkt.
	Bank G	No	Moderate	Moderate	No
	Bank H	No	Moderate	Low	No
	Bank I	No	Low	Low	No

* Shown as a percentage of small business loans on the books.

A Low = $100K or less; Moderate = $100K–250K; High = greater than $250K

B Low = less than 10%; Moderate = 10–50%; High = 50% or greater

Institutions shown towards the top place greater reliance on the scoring models. In other words, they are more liberal users of the models. Those listed toward the bottom are more conservative users. Based on this survey group, it appears that the longer an institution uses scoring, the more liberal their usage becomes.

Performance of scored loans: The respondents all indicated that the performance of scored loans has been at least as good as expected, with most reporting "better than expected" performance. Five also believe that their scored loans have outperformed their non-scored loans in terms of charge-offs and delinquencies, although to some, this could also be a function of an improved economy. One respondent reported that scored loans have underperformed non-scored loans, although this lender is still satisfied with its scoring system results.

Why scoring is used: Lenders that use scoring models claim several benefits: 1) faster loan decisions, 2) substantial efficiencies, and 3) improved underwriting consistency across an entire organization.

Why other institutions don't use scoring: Many of the forty-two respondents that do not use scoring models for small business lending prefer to give individual attention to each loan request. They feel that scoring would interfere with the existing culture of the institution, which emphasizes close customer relationships. Many also reported cost as a factor, citing an insufficient scale of business lending to justify the expense of a scoring model.

Loan Growth of Scorers Versus Non-Scorers

With the efficiencies made possible through credit scoring, we wanted to find out if scoring users are "cornering the market" on new small business loan originations.

While there is some evidence that scoring users are able to expand their small business lending at a rapid pace, the non-scorers are also generating new small business loans. Based on our sample, the growth rate of small business loans at institutions using scoring was a healthy 11% between 6/98 and 6/99. Over the same period, non-scorers grew their small business loans by 6%.[1] While this is a lower growth rate than that of the scorers, it does indicate that, at least for this group of western banks, small business loan expansion opportunities still exist for those that do not use scoring.

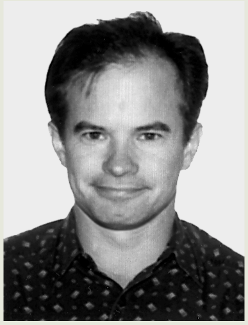
Fair Lending Implications

Scoring models can have positive fair lending impacts. A properly constructed model avoids using any variable that is among the prohibited bases[2] in Regulation B. A scoring program can therefore, help reduce fair lending risks to lenders and facilitate an equitable expansion of credit access.

However, a model must be empirically derived and demonstrably and statistically valid to qualify as a credit scoring system under Regulation B. Otherwise, the system is considered "judgmental," which removes certain "safe harbor" protections such as the limited inclusion of applicant age in the model, and necessitates a more thorough fair lending review.

1 *Based on small business loans with original maturities of $250 thousand or less.*

2 *Prohibited bases include: national origin, age, gender, marital status, race or color, religion, receipt of public assistance.*



About the Author

Gary Palmer has nearly 20 years of experience at the Federal Reserve Bank of San Francisco. He currently serves as banking studies officer in the Division of Banking Supervision and Regulation. Mr. Palmer's recent work has focused on researching emerging issues and trends within the banking industry. Previously, he served as information technology officer and as financial analysis officer within the Division. Mr. Palmer holds an M.B.A. degree from the University of California at Berkeley and is a graduate of the Pacific Coast Banking School in Seattle.

Additionally, even a qualified credit scoring system does not eliminate fair lending concerns. For example, lenders often allow for a limited volume of overrides in their use of scoring models. Care must be taken to ensure that reasons for overrides are objective and nondiscriminatory; the reasons for the overrides should then be documented. Lenders should also track the performance of overrides.

Conclusions and Next steps

It is evident that small business lending is now dominated by lenders that use credit scoring models, and that scoring is continuing to attract new followers for cost and competitive reasons. It is also clear that the vast majority of these lenders use models from one vendor, and that the fair lending implications of these models appear to be mostly positive.

The Federal Reserve is continuing to research issues related to credit scoring. Some of the areas of possible further research include:

- Evaluating the variables and methodology used by the popular scoring models;
- Obtaining information on the application integrity risk controls in place by vendors and credit bureaus to prevent the distribution of erroneous information;
- Looking at how lenders validate the models they use to ensure that the scoring systems are leading to appropriate decision-making;
- Considering the implications of scoring on credit risk at individual institutions and the entire banking industry;
- Considering differences in regulatory risks faced by lenders based on their selection of vendor or home-grown models. ***CI***

For more information on this survey or future Fed research please call Gary Palmer at (415) 974-3003.

Creating CULTURAL WINDOWS to Banking OPPORTUNITIES

By Gilda Haas, Executive Director,
Strategic Actions for a Just Economy

THERE IS A RECURRING CONDITION IN THIS COUNTRY'S ECONOMIC LANDSCAPE THAT LEAVES LARGE SEGMENTS OF OUR POPULATION SITTING ON THE SIDELINES. The underserved market to which I refer represents enormous, yet still untapped, economic potential. It includes individuals who are systematically lumped into the "unbanked" category; a catch-all word that carries so many stereotypes and so much baggage, it's just easier to ignore it altogether.

The numbers are economically significant. Approximately 1 million new immigrants enter the United States each year. The majority come from Asia and the Americas, and as a result, Los Angeles has replaced New York as the primary point of entry into this country. Although there are new immigrants living in cities and towns across the nation, many regard L.A. as a "living laboratory" . . . the perfect place to study and better understand immigrant issues. In L.A., for example, one out of three residents is foreign born, and the area's cultural diversity is so great that 79 different languages are spoken in the L.A. Unified School District.

> *"The numbers are economically significant. Approximately 1 million new immigrants enter the United States each year."*

Strategic Actions for a Just Economy (SAJE) is a community-based organization in Los Angeles that is dedicated to improving opportunities for working-class people and new immigrants. The organization's banking experience began back in 1988, when activists, who are now part of SAJE's banking program, organized to fight branch closings in South Central LA.

More recently, SAJE has launched an ethnic banking project to learn more about the banking practices and economic potential of immigrant groups. The pilot study has generated financial profiles of four immigrant communities—Armenian, Korean, Salvadoran and Cambodian. More studies are planned, but these initial four provide a basic foundation of knowledge, a methodology, and a platform upon which to build a much larger view of the impediments to and possibilities for banking L.A.'s diverse ethnic consumers.

Lessons From The Study

Banks that are interested in playing a larger role in the financial lives of new immigrants may borrow some lessons from the SAJE study. There are obvious communication efforts that can be made, such as hiring staff who speak the language, both literally and culturally, and providing materials in languages other than English. But to learn how banking issues interface with the immigrant experience requires flexible thinking.

A good starting place is to look at boilerplate requirements that most banks use to determine the stability and creditworthiness of their customers. In the case of new immigrants, these requirements may simply be missing the mark, and with it, opportunities for communities as well as financial institutions. Questions to pose, are "what do we really need to know?" and, " Is their another way to achieve the same results?" Concrete action steps for banks to consider include:

➤ Develop flexible identification requirements

Bank accounts are a basic point of entry to the financial mainstream of the U.S., but the requirement to provide credit cards and/or multiple forms of photo identification often preclude the ability of newcomers to open a bank account. SAJE has worked with several banks to identify what they really need to know about people, and to develop alternative identification requirements that meet the banks' needs and are more feasible for our constituents.

➤ Take a more flexible approach to evaluating credit history and creditworthiness

Establishing a credit-history is difficult for most first-generation immigrants, even through they may have excellent credit records in their country of origin. The fact that a person or organization has been operating successfully outside the U.S. financial mainstream could be seen as an asset rather than a liability. More respect should be paid to financial success in another country as a valid credit history. An alternative is to accept non-traditional forms of credit history—consistent and timely payment of bills, for example, over a substantial period of time.

➤ Develop flexible strategies that increase loan opportunities for immigrants

Cultural adaptations are the key components of successful programs that build and extend credit to new immigrant populations. Korean banks, for example, have helped their customers build credit histories by establishing installment savings accounts that borrow from Korean cultural practices. Autofin, described later, incorporates the familiar *tanda* process in an institutional lending setting. These are not dissimilar from Christmas Clubs and other traditional American banking products, yet are designed to resonate with the experience of immigrant consumers.

This type of thinking and approach actually opens doors for all under-served people, native Americans and immigrants alike. Indeed, one of the great advantages of accomodating immigrants is how it accomodates the rest of us as well. The following story illustrates how cultural traditions can be adapted to U.S. banking practices in order to reap substantial collateral benefits.

The Story of Autofin

Autofin is a large Mexican finance company with over 60,000 customers. The company's lending strategy is designed to capitalize on *tanda*, a traditional, informal lending circle typically used by women in Mexico to pool resources for "once in a lifetime" expenses such as weddings, quinceneras, or funerals.

Autofin has adapted and formalized the concept so that applicants enter an established lending group defined by the loan amount they are seeking. Autofin, like tanda, requires participants to make monthly contributions to a common fund prior to actually applying for a loan. This way, potential applicants build up savings while establishing a "repayment" history at the same time. After a minimum number of payments into the loan pool, applicants are able to receive car, home, or business loans. But now, instead of making monthly contributions to the pool, they are making monthly loan repayments, under much the same terms as before.

The Autofin story describes how traditional banking products such as savings clubs and secured loans can be adapted to emulate cultural practices around lending and money. This is a relatively new concept for U.S. banks, which adapt to cultural contexts in order to compete in foreign markets, but still shape their domestic products around a white, middle-class consumer model.

Today, substantial "foreign markets" reside in American cities. SAJE plans to continue the ethnic banking project to learn more from other, diverse communities in L.A. Based on our past experience, we are confident that merging the culture of banks with that of new immigrant communities can result in great opportunity and significant potential for both. ***CI***

SAJE's ethnic banking study entitled "Transactions: Building Access to Financial Services and Credit Across L.A.'s Immigrant Communities" *is available free of charge. SAJE is actively soliciting partnerships with banks that wish to develop innovative, culturally responsive strategies for serving immigrant populations. For a copy of the report or additional information, please contact Gilda Haas, executive director, at (323) 732-9961.*

SAJE

Strategic Actions for a Just Economy

SAJE is a 501(c)3 corporation founded on the premise that many of Los Angeles' social problems have economic roots. Our primary mission is to build economic power among grassroots people. SAJE's strategy is a bottom-up approach that convenes people affected by a problem and helps them create solutions with others at a much greater scale.

Our unique contribution to community development in Los Angeles is our focus on the relationships between ownership, capital and participation. Towards this end, SAJE's core programs promote access to banking services, the development of sustainable jobs through cooperative enterprises, and the creation of public policies that make capital more accountable to community and worker needs.

Recent Accomplishments

SAJE has been building new economic options for working class people in Los Angeles since our inception in 1994. In addition to our ethnic banking project, some of our accomplishments include:

➤ *Welfare-to-Work Banking:* SAJE has created a partnership among community reinvestment activists, welfare recipients, advocates, L.A. County's Department of Social Services, and Washington Mutual Bank to create the County's first direct-deposit policy and a welfare-to-work bank account that may ultimately serve thousands of people on aid in L.A. County. Presently in the pilot stage, the program anticipates federally mandated electronic benefit transfer laws that must be implemented across the country by the year 2001. It will provide an alternative banking model for people who are being mainstreamed from welfare checks to paychecks.

➤ *Cooperative Job Development:* SAJE has organized immigrant low-wage workers into cooperative job development programs that provide alternatives to exploitative working conditions, provide living wages, and a sustainable foundation for the future. To date, our *Hollywood Domestic Workers Cooperative* has generated over 200 housecleaning jobs which pay an average of $10 per hour.

➤ *Healthy Homes Collaborative:* SAJE is the lead organization of a collaborative which includes Esperanza Community Housing, St. John's Well Child Clinic, and L.A. County's Childhood Lead Poisoning Prevention Program. The project seeks to prevent lead poisoning in SAJE's own "lead hot spot" neighborhood by integrating housing, health, and employment initiatives into a comprehensive approach. We have recently trained 15 neighborhood residents as State-certified lead abatement workers and are building a foundation for a more strategic lead abatement policy in L.A.

For more information, please call or write us:
SAJE, 2636 Kenwood Avenue, Los Angeles, CA 90007, (323) 732-9961

About the Author

Gilda Haas is an organizer, educator, and economic development professional who has been assisting community and labor organizations in building economic development projects and policies from the ground up for over twenty years. She is the director of Strategic Actions for a Just Economy (SAJE), an organization dedicated to building economic power for working class people in Los Angeles.

Ms. Haas' contributions to economic development are varied. She founded Communities for Accountable Reinvestment, a diverse coalition based in Los Angeles that fights against redlining and for community development banking. She was also founding Board member of South Central People's Federal Credit Union. Ms. Haas also created the Community Scholars Program, housed in UCLA's School of Public Policy and Social Research, where she has taught economic development courses for the past 15 years. Congress has tapped Ms. Haas' expertise numerous times by requesting her testimony on community banking issues.

HOME FOR DINNER HOME BUYERS PROGRAM

Finding a Way to Increase Homeownership Opportunities for Las Vegas Employees

By Joselyn A. Cousins, Vice President, Community Development Banking, Bank of America Nevada and Doreen Davis-Peterson, Community Investment Manager, U.S. Bank Nevada

The Las Vegas Valley is home to thousands of companies that employ low- to moderate-income wage earners. Visitors are often amazed by the sheer number of dealers, waiters, parking attendants, and others who work hard to maintain the city's reputation as America's greatest play land. While hourly wages tend to be low in the hospitality industry, employees fare pretty well—mainly because tips supplement their low pay. But in the large urban valley that exists beyond the Strip, there are hundreds of other companies where tips aren't part of the trade. For employees of these companies, their paychecks are often their sole source of income.

Employment opportunities at all levels of the income scale have fueled explosive population growth in the Las Vegas area. As a result, the ratio of renters to owners has reached an all-time high. Nevertheless, Las Vegans continue to place a high priority on home ownership, and the development of affordable, single-family housing is a prevalent lending activity for many financial institutions operating in Southern Nevada.

Affordable mortgages are also high on the area's priority list, again fueled by population growth. But banks have struggled with how to effectively reach and serve a potentially profitable segment of the market . . . the thousands of low- and moderate-income wage earners slowly being shut out of the Las Vegas housing market.

CRA Officers Take the Lead

To address this growing problem, a small group of CRA officers met in April 1997, and discussed ways to better capture Las Vegas' lower wage market. After researching various programs around the country, the team decided to pursue the creation of an employer-assisted housing (EAH) program. The program, which eventually came to be known as the "Home for Dinner Home Buyers Program," would have four important components:

- ➤ a sponsoring employer with a base of at least 1500 employees;
- ➤ a home owner education and credit counseling component;
- ➤ down payment assistance options for qualifying borrowers; and,
- ➤ affordable mortgage products, with rates that could be offered below market.

At the outset of the effort, casinos headquartered in both Reno and Las Vegas were targeted as sponsoring employers, an obvious first choice in Nevada. But the team found little success with the gaming industry. In late 1998, the Nevada Fair Housing Center (NFHC) joined the planning effort, and several non-gaming employers were identified as Home for Dinner prospects.

Meanwhile, the mortgage divisions of participating banks were busy identifying and creating affordable lending products for the Home for Dinner program. By February 1999, the lending products were in place, and the role of each program partner was clarified. With these steps completed, the planning team was ready to share its Home for Dinner program with three target employers, two of which were local governments, and the other, a credit card bank with a large back-office operation in Southern Nevada.

Household Bank Accepts the Concept

Seizing an opportunity to fulfill investment test requirements under the Community Reinvestment Act, Household Bank decided to pilot the program and market it to its Las Vegas employees. But this decision was not without its set of challenges and limitations.

The primary challenge was how to participate in the down payment assistance piece without violating employee benefits law. At its most basic level, the law requires that all non-salary related benefits be made equally available to employees of a corporation. Since Household has offices and staff in other states, and because the program targets those earning 80% or less of area median income, management determined that its participation would have to be "invisible" to employees. Since down payment grants were not an option, an additional partner was needed to complete the puzzle.

In August 1999, a local community bank, BankWest of Nevada, joined the initiative, agreeing to offer second deed of trust loans that could be used for down payment or closing costs. Household agreed to deposit $50,000 in a BankWest CD account, which effectively eliminated the interest on the second deed of trust loans for a period of five years. With these final pieces in place, the Home for Dinner Home Buyer's Program was ready to go. Household began internal marketing of the program, and the first informational sessions were held in the fall of 1999.

Outreach to Potential Home Owners

Ninety-five Household employees attended the first session of the Home for Dinner Home Buyers program. Representatives of the three participating mortgage lenders—Bank of America, U.S. Bank and Wells Fargo - along with team members from Nevada Fair Housing Center and Consumer Credit Counseling Service presented the EAH concept. Presentations included an overview of the program, homeownership education requirements, and steps in the mortgage lending process.

It is not yet known how many of those first 95 will proceed through the program and qualify for a mortgage. The estimated time for completion is anywhere from 1–12 months, depending on the condition of the applicant's credit. And, although the program is targeted to serve people earning from 50-80% of the area median income, the team is committed to offering it to anyone interested in pursuing home ownership.

This commitment is demonstrated by the critical roles played by the Nevada Fair Housing Center and the Consumer Credit Counseling Service. In addition to leading the educational effort, the NFHC received a program grant from the U.S. Department of Housing and Urban Development to serve in a liaison capacity for participants who need one-on-one assistance throughout the entire process. If requested, NFHC staff will guide participants through every step to ensure that nobody "gets lost in the shuffle." For those with weak credit, Consumer Credit Counseling Service is on-hand to provide free credit counseling and credit repair.

The Future of the Program

After the initial round of sessions are complete, the Home for Dinner team will meet to discuss next steps for the program. Topics for discussion will likely include outreach to additional Las Vegas employers and the creation of non-profit partnerships to expand down payment and closing cost options. In the meantime, hundreds of Household Bank employees will be building a financial edge for their futures and contributing to the stability of the neighborhoods they choose to call home.

Roles of Home for Dinner Partners

Bank of America, U.S. Bank, Wells Fargo

➤ Provide first mortgages, using specially designed loan products with favorable terms.
➤ Present the program to Household Bank employees at series of informational sessions.
➤ Work with potential clients to help them understand various mortgage loan programs and the loan process.

BankWest of Nevada

➤ Provide a loan secured by a second deed of trust to assist the employees of Household Bank with down payment and/or closing costs.

Household Bank

➤ Provide access and marketing to employees.
➤ Provide space at their facilities for informational and education sessions associated with the program.
➤ Deposit $50,000 in a CD account to write-down the seconds offered by BankWest of Nevada.

Nevada Fair Housing Center & Consumer Credit Counseling Service

➤ Determine eligibility of each employee and, when appropriate, refer them to Consumer Credit Counseling Service for pre-purchase credit preparation.
➤ Lead home buyer education sessions, provide credit and post-purchase counseling for employees who participate in the program.
➤ Serve in a liaison capacity for participants seeking one-on-one assistance throughout the process. *CI*

For more information on the Home for Dinner Home Buyers Program, please contact Joselyn Cousins at Bank of America Nevada (702) 654-7848, Doreen Davis-Peterson at US. Bank Nevada (702) 688-3565, or Steve Linder at Household Bank (702) 243-1390.

About the Authors

Joselyn Cousins is a vice president in Community Development Banking at Bank of America in Nevada. Ms. Cousins is responsible for the organization's performance under the Community Reinvestment Act. She administers the Community Reinvestment Act program through partnerships with community group representatives and Bank of America senior management.

Ms. Cousins began her banking career in 1986, and has been a member of the Bank of America team since 1993. She was appointed to her current position in 1994. Her past roles includes residential lending, construction lending and retail banking.

Ms. Cousins currently serves on several boards including North Las Vegas Neighborhood Housing Services, Nevada MicroEnterprise Initiative and the Community Development Recommending Board for the City of Las Vegas. She attended California State University, San Bernardino and holds a B.A. in Administration.

Doreen Davis-Peterson is vice president and manager of U.S. Bank's Community Investment Department in Nevada and Utah, responsible for assuring the organization's compliance with the objective and technical requirements, and implementation of the federal Community Reinvestment Act. In addition, she manages community relations for U.S. Bank in both states, including corporate philanthropy, employee volunteerism, and community partnerships.

Ms. Davis-Peterson began her banking career in 1977. She joined U.S. Bank in 1992, was named CRA manager in 1993, and undertook the community relations function in 1999. Ms. Davis-Peterson has also held roles in lending, credit analysis, branch management and customer service.

Ms. Davis-Peterson currently serves on the Advisory Board of the Ethnic Student Resource Center at the University of Nevada, Reno and is an appointed member of the Nevada State Department of Human Resources Block Grant Commission. She holds an A.A. from Truckee Meadows Community College and is currently attending the University of Nevada, Reno.

Micropolitan Community Reinvestment Trusts

By Kevin O'Brien, President, Sovereign Capital, Inc.

Financial Institutions face unique challenges in complying with the CRA in smaller "micropolitan" communities where there are few investment opportunities with acceptable portfolio risk. Opportunities that can be found tend to be characterized by high levels of distressed infrastructure.

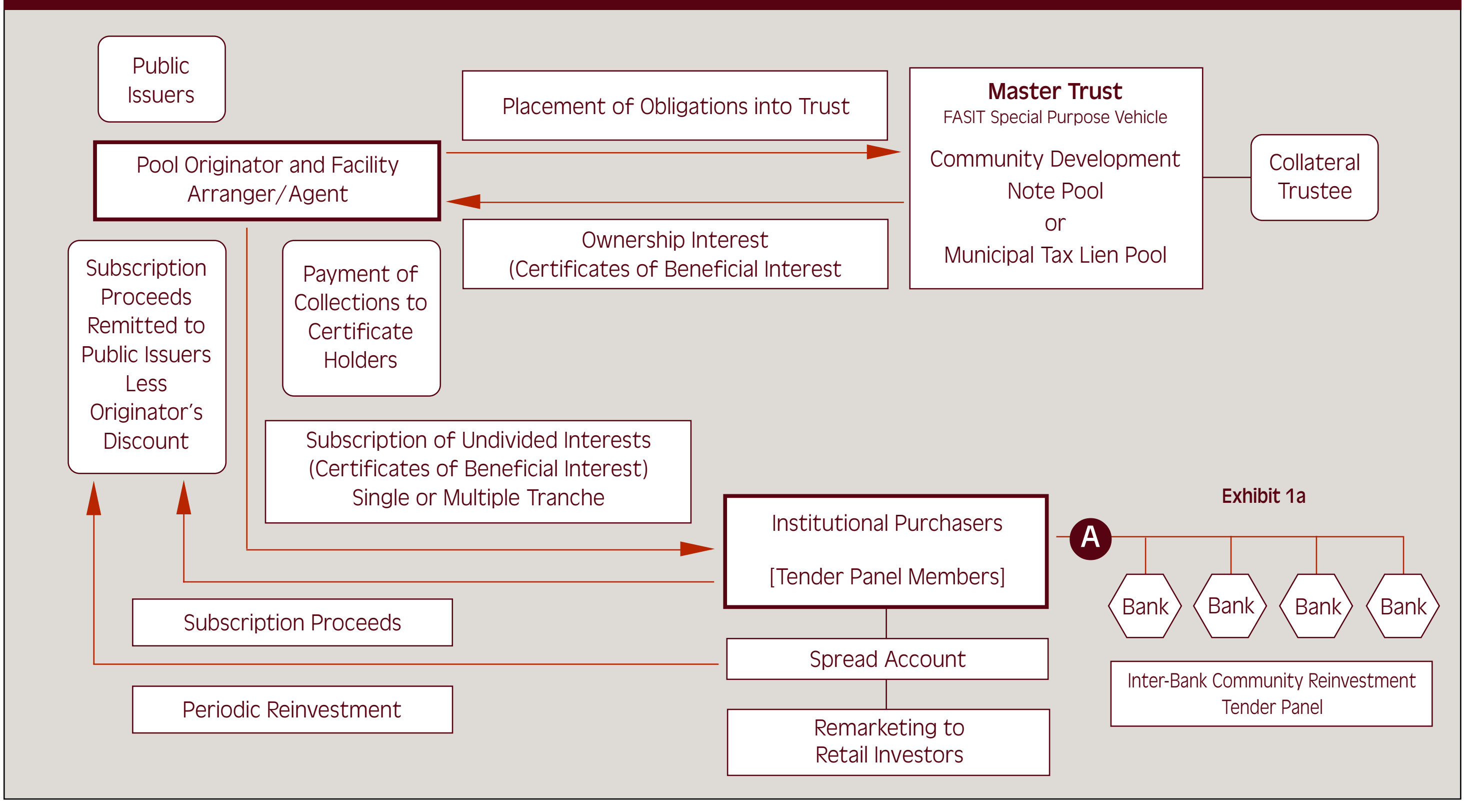
Small municipal governments face their own challenges in financing community facilities and making physical improvements. The costs of debt rating and issuance of debt are frequently prohibitive because of relatively small-sized bond issues in micropolitan areas.

> *"This article offers a potential solution for both financial institutions and small community governments: special asset securitization trusts."*

This article offers a potential solution for both financial institutions and small community governments: special asset securitization trusts. These trusts, while still in a conceptual phase, could operate as revolving debt pools for small cities.[1] Small city governments, special districts, schools, hospitals and other taxing jurisdictions could collectively issue debt obliga-

1 *The IRS allows for the creation of trusts that securitize pooled debt obligations. These obligations are treated as debt for federal income tax purposes so that interest is deductible.*

Community Reinvestment Trust Operating Structure



tions and realize substantial savings in debt rating fees, underwriting costs, and interest expenses, since such costs would be shared among pool participants. Collectively, these municipalities could reduce their interest costs since diversification would improve their credit profiles and since "quality of life," indicators, which are generally high for small cities, could be considered as rating criteria.

Financial institutions could choose either to sponsor or invest in these trusts. Sponsors would create the trusts and could originate bridge loans, secured by tax anticipation notes, which would initially fund the trusts. Municipalities would, of course, place their yet-to-be-subscribed obligations into the trusts.

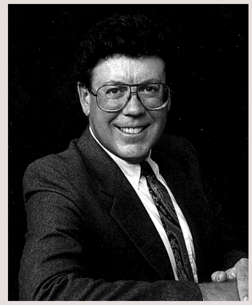
Investors, including financial institutions, would then purchase "community reinvestment certificates" issued by the trusts, much as they would purchase securitized packages of credit card receivables or automobile loans. This same process could apply for the sale of securitized municipal tax liens, which are projected to grow at $5 billion per year.

Besides sponsoring trust obligations or investing in certificates, financial institution representatives could choose to serve on "inter-bank tender panels" which would periodically review certificates issued by the trusts or review offering memoranda describing specific issues.

In addition to favorable customer and public perception, financial institutions could benefit from CRA investment test consideration since products designed to finance community and economic development initiatives sponsored by local governments qualify. Also, investment interest income from subscription of community reinvestment certificates and reduced portfolio volatility through diversification of credit risk would be advantages. Sponsoring financial institutions would also have the capability to earn financial advisory and facility fees. Finally, sponsoring banks could create bridge funds to provide small city issuers with interim financing before obligations are securitized, generating an additional source of fee revenue. Investing institutions could hold these obligations for their own accounts or could re-price them for retail distribution as individual investor account products.

Through participation in this program, financial institutions could directly and profitably facilitate community development projects within targeted lending markets, creating foundations for future profitability from population and business growth through development of local and regional credit markets. The trusts could also improve access to capital for economically disadvantaged communities and ensure availability of financial resources for small communities across America. ***CI***

If you are interested in pursuing this idea, please contact Kevin O'Brien at Sovereign Capital, Inc. in Tucson, Arizona. Tel: (520) 615-4525 / Fax: (520) 749-3304.



About the Author

Over the past sixteen years, **Kevin O'Brien** has worked in both corporate and economic development finance. As an investment banking professional in California, Mr. O'Brien specialized in emerging market transactions, debt conversion finance and special situations, and participated in the creation of special purpose vehicles utilized in the issuance of asset-backed securities and other specialized financial structures. As president of Sovereign Capital, Inc., Mr. O'Brien pioneered the creation of First Nations and small city economic development finance programs, including creation of a regional air service program to benefit underserved communities. He also developed the Exitbond® program for increasing private investment on Native American reservations. Mr. O'Brien holds a Bachelors degree in Finance from Northern Arizona University.

2000 Community Reinvestment Conference

April 16-19, 2000
Palace Hotel, San Francisco

Daily Schedule

(Please refer to conference brochure for more details.)

Sunday, April 16

3:00 p.m.	Executive Briefing Leadership Council Meetings
5:00 p.m.	Leadership Council Reception

Monday, April 17

8:00 a.m.	Registration and Breakfast
10:00 a.m.	Opening Session *Ellen Seidman, OTS* *Angela Blackwell, PolicyLink*
12:00 noon	Lunch and Keynote Address *Edward Gramlich* *Federal Reserve Board*
1:30 p.m.	Concurrent Training Sessions
5:00 pm	Speaker's Reception/ Free Evening

Tuesday, April 18

7:30 a.m.	Networking Breakfast
8:30.a.m.	Concurrent Training Sessions
11:45 a.m.	CRA Awards Presentation
12:30 p.m.	Lunch and Speaker *Scott Morgan, DreamBuilders*
1:30 p.m.	Concurrent Training Sessions
5:00 p.m.	Showcase Reception

Wednesday, April 19

7:30 a.m.	Networking Breakfast
8:30.a.m.	Concurrent Training Sessions
11:30 a.m.	Closing Address *Donna Tanoue, FDIC (invited)*
12:00 noon	Lunch: Special Commonwealth Club Presentation: *The Future of CRA*

Win a Free Registration and The Spotlight at the 2000 Community Reinvestment Conference

The Federal Home Loan Bank of San Francisco and the Federal Reserve Bank of San Francisco are pleased to invite financial institutions to participate in a *Products and Services Awards* competition. The awards program is an effort to recognize and share innovative and outstanding examples of CRA-eligible products or services in the categories of lending, service, investment and community development. Entries in any or every category will be accepted until February 15, 2000.

Entry information was sent out in mid December. If you did not receive it or would like more detailed information, please contact Lena Robinson at (415) 974-2717 or by e-mail at **lena.robinson@sf.frb.org**.

Training Sessions At-a-Glance

Training Track	Monday Afternoon	Tuesday Morning	Tuesday Afternoon	Wednesday Morning
Profiles of Compliance	Overview of CRA Exam Techniques	Small Bank Exam & Large Bank Exam	Community Development Service & Investment	Safety & Soundness for CRA Officers
Community Development Finance	Small Business Lending	Single Family Housing Development	Multi-Family Housing & Mixed-Use Developments	Finding the Common Ground for Development Lending
Community Development Investments	Bank Treasury Training for CRA Professionals	Equity Investments	Deposits & Grants/ Corporate Giving Strategies	Fixed Income Securities
Community Building	Profile of a Community: Site Visit to Eastmont	The Unbanked – Serving Emerging Markets Responsibly	Profile of a Community: Site Visit to The Tenderloin	Serving Rural and Native American Communities

CRA Conference brochures with detailed session and registration information will be mailed in mid January. Contact Lena Robinson at (415) 974-2717 if you do not receive a brochure or if you would like more information.

Bulletin

Toward a Sustainable America

The President's Council on Sustainable Development (PCSD) has released *Toward a Sustainable America: Advancing Prosperity, Opportunity, and a Healthy Environment for the 21st Century*. This report updates PCSDs 1996 version, and includes current policy recommendations. It highlights the council's objective to improve prosperity and quality of life while reducing human pressures on the environment. Appendices include examples of successful community initiatives, resources, and council member profiles.

For more information or a copy of the report, contact the PCSD at (202) 408-5296 *or at* **www.whitehouse.gov/PCSD**.

Economic Education Program Satisfies CRA Criteria

Bankers may want to consider Junior Achievement's (JA) innovative, economic education program as one option in fulfilling their CRA requirements. JA programs are designed to train students from kindergarten through 12th grade with work-force-ready economic skills and knowledge. The majority of the programs are delivered to low-income students.

One of JA's primary programs is called the **Whole School Program**. Banks and businesses may fund classrooms, whole grades, or adopt an entire school. Banks can receive Investment Test credit when they provide funding to sponsor a Whole School Program in a low-income neighborhood. They can also receive Service Test credit if their employees volunteer in the sponsored school.

For more information about Junior Achievement programs, contact Senior Development Manager, Julie Ringwood, at (323) 957-1818, ext. 20.

New Web Site Links Projects to Programs and Resources

1stSource is a new Internet site launched in October by the Federal Reserve Bank of Kansas City. The site is a guide to information about programs that assist community and economic development projects. Whether you are a developer trying to build affordable housing, a small business entrepreneur seeking financing, a small farmer operating a farm, or a community seeking to improve its infrastructure, **1stSource** can help you easily and quickly cut through the maze of programs. With a little information from you about your project, **1stSource** will provide you with a summary description of those programs that best fit your project's needs.

The site is **http://www.1stsource.kc.frb.org/programs/index.asp.** *For more information, call John Wood at the Federal Reserve Bank of Kansas City at* (800) 333-1010, ext. 2203.

The Social Entreprenurial Fund (SEF)

In its first two years of operation, the Social Entrepreneurial Fund (SEF) of the Liberty Hill Foundation has distributed over $300,000 in grants to nine non-profit and/or worker-owned micro-enterprises in low-income communities of Los Angeles. Based on lessons learned from this non-profit program, Liberty Hill is ready to proceed with micro-loans to private entrepreneurs in low-income areas for sustainable business ventures. They are seeking matching investment funds from banks for a loan pool, as well as grants for technical assistance.

For more information, please contact Michele Prichard, director of Special Projects at (310) 453-3611, ext. 104.

CRA Leadership Councils

January 7, 2000 is the final day to submit a nomination form for the CRA Leadership Council. The Leadership Councils are a voluntary advisory board of CRA officers who will serve as representatives of their local roundtable. For further information on the program or to receive a nomination packet, please call Lena Robinson at (415) 974-2717 or contact her via e-mail at: **lena.robinson@sf.frb.org**.

Free Compliance Chat Group

With *Regulatory Risk Monitor's* compliance listserv, you can pose your toughest questions to colleagues and get speedy replies offering insight, experience and useful tips on CRA, staff training, fair lending, credit scoring, regulatory requirements and safety and soundness issues. You may even be the one who can respond to a colleague's challenge!

It's easy to subscribe. Just send an e-mail to: Majordomo@user-home.com. Leave the subject line blank. In the message section, type: **subscribe compliance**. Please don't include a signature file. Just hit the reply button, send back the message, and you're done!

For further information, call Regulatory Risk Monitor's *Executive Editor Fran Fanshel at (800) 929-4824, ext. 2245.*

2000 CRA Roundtable Dates

Financial institution CRA officers and bank community development staff are invited to participate in the Roundtables. These meetings are valuable sources of information about CRA regulatory compliance and about local community credit, service and investment opportunities.

City	1st Quarter	2nd Quarter	3rd Quarter	4th Quarter
Boise	March 9	June 8	September 14	December 14
Greater Los Angeles	February 9	May 17	August 9	November 8
Las Vegas	March 14	June 13	September 12	December 12
Northern California	February 8	May 9	August 8	November 7
Phoenix	March 23	June 22	September 18	December 14
Portland	January 4	April 4	July 6	October 3
San Diego	Date TBD	TBD	TBD	TBD
Seattle	February 10	May 18	August 10	November 9
Utah	January 13	TBD	TBD	TBD

Community Affairs Contacts for Roundtables:

Adria Graham Scott (213) 683-2785 (Los Angeles, Phoenix, San Diego)

Fred Mendez (415) 974-2722 (Northern California, Las Vegas, Utah)

Craig Nolte (206) 343-3761 (Boise, Portland, Seattle)

Lena Robinson (415) 974-2717 (Leadership Councils)

Free subscriptions and additional copies are available upon request from the Community Affairs Unit, Federal Reserve Bank of San Francisco, 101 Market Street, San Francisco, California 94105, or call (415) 974-2978.

Change-of-address and subscription cancellations should be sent directly to the Community Affairs Unit. Please include the current mailing label as well as any new information.

The views expressed are not necessarily those of the Federal Reserve Bank of San Francisco or the Federal Reserve System. Material herein may be reprinted or abstracted as long as *Community Investments* is credited. Please provide the Managing Editor with a copy of any publication in which such material is reprinted.

Seasons Greetings from the Staff of Community Affairs

Federal Reserve Bank of San Francisco
101 Market Street
San Francisco, CA 94105

Address Service Requested

FIRST CLASS MAIL
U.S. POSTAGE
PAID
PERMIT NO. 752
San Francisco, CA

Attention:

Chief Executive Officer
Compliance Officer
CRA Officer
Community Development Department