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Public welfare investment cap increased to 20%: What it means for banks, syndicators, and the LIHTC equity market

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The 21st Century ROAD to Housing Act raises bank public welfare investment caps, expanding capacity for LIHTC, CRA, and affordable housing deals.

What's the impact?

- Banks approaching the prior 15% cap may now have more capacity for LIHTC, NMTC, historic tax credit, and other CRA-related investments.
- The Community Investment and Prosperity Act increases the cap for certain bank public welfare investments to 20%.
- Syndicators and fund sponsors may see new opportunities as banks evaluate how to deploy added capacity for affordable housing and community development.

Congress recently passed the 21st Century ROAD to Housing Act (the Act), a broad housing supply and affordability package that includes a targeted but potentially meaningful change for investors in affordable housing and other community development investments. Section 203 of the Act, titled the Community Investment and Prosperity Act, increases the statutory cap on certain bank public welfare investments from 15% to 20% of capital and surplus. The change applies to investments made by both national banks and state member banks under the applicable statutory authority. The amendment may provide additional balance sheet capacity to support future Community Reinvestment Act (CRA) investments for banks that are active investors in low-income housing tax credit projects, historic tax credit projects, new markets tax credit transactions, small business investment company funds, housing preservation funds, certain workforce housing investments, and similar investments. Importantly, the increase comes at a time when Congress has also expanded the low-income housing tax credit (LIHTC) program, making additional private investment capital increasingly important to finance future affordable housing production.

Background

Federal banking law has long authorized national banks and state member banks to make "public welfare investments" designed primarily to benefit low- and moderate-income communities. That authority forms the basis for many bank investments in affordable housing and other community development initiatives, including investments in LIHTC projects, New Markets Tax Credits (NMTC), Historic Tax Credits, and other qualifying CRA-related investments. For national banks, the authority appears in the paragraph designated "Eleventh" of 12 U.S.C. § 24, which authorizes national banking associations to make investments designed primarily to promote the public welfare, including the welfare of low- and moderate-income communities or families, creating housing, services, jobs, or other community benefits to these populations. For state member banks, a parallel authority appears in Section 9(23) of the Federal Reserve Act, codified at 12 U.S.C. § 338a. Public welfare investment authority is commonly used to support investments in:

- LIHTC equity;
- Affordable housing preservation and production vehicles;
- NMTC investments;
- Historic tax credit projects with community development characteristics;
- Investments in small business investment companies and rural business investment companies; and
- Investments supporting low-income and moderate-income communities, services, or job creation.

Prior to enactment of the Act, a regulated bank generally may make public welfare investments up to 5% of capital and surplus without exceeding the baseline statutory threshold. With approval or non-objection from the relevant federal banking regulator, a bank may exceed that 5% level, subject to an aggregate statutory ceiling. Before the Act, that ceiling was 15% of capital and surplus.

Section 203 of the Act amends two statutes. First, it amends 12 U.S.C. § 24, Eleventh, by striking "15" each place it appears in the relevant sentence and replacing it with "20." This increases the maximum aggregate amount of public welfare investments by national banks from 15% to 20% of capital and surplus. Second, it makes the same change to Section 9(23) of the Federal Reserve Act, 12 U.S.C. § 338a, increasing the corresponding cap for state member banks from 15% to 20%. The Act also creates a new reporting requirement. No later than two years after enactment, and every two years thereafter, the OCC and the Federal Reserve must each submit reports to Congress regarding public welfare investments made during the prior two calendar years. Those reports must identify the number and dollar amount of investments, broken down by purpose, type, bank size, and geographic location. The new reporting requirement suggests that Congress intends to monitor how financial institutions utilize this additional investment authority and whether it translates into increased community development investment.

Potential implications for investors

The public welfare investment cap can be a particularly binding constraint for institutions with large or mature community development investment portfolios. By increasing the cap from 15% to 20%, Congress has provided additional regulatory capacity for banks approaching the prior statutory limit. For banks already approaching the 15% ceiling, the change may allow those institutions to continue making tax credit and community development investments without needing to curtail new commitments, sell existing positions, or wait for capital growth to create additional room. For banks not currently near the cap, the amendment may influence longer-term capital planning, CRA strategy, and affordable housing investment appetite generally.

The timing of this amendment is also significant. Congress recently expanded the LIHTC program through the One Big Beautiful Bill Act, which is expected to increase the amount of equity capital needed to finance affordable housing developments over the coming decade. While the increase in the PWI cap does not create additional investment demand, it removes one regulatory constraint that may allow certain banks to deploy additional capital to qualifying community development investments, including LIHTC transactions.

Generally, this additional capacity could be used for any number of the CRA-related investments noted above. Although the expanded authority may be used for a broad range of qualifying community development investments, increasing affordable housing investment appears to have been one of Congress's principal objectives.

Will this change lead to a dollar-for-dollar increase in the LIHTC equity market, placing upward pressure on tax credit pricing? Not necessarily, as demand (and therefore pricing) still depends on several additional factors, including: (a) whether a bank is actually constrained by the current cap, (b) the availability of desirable projects, (c) CRA strategic value, (d) the investor's tax appetite and interest rate assumptions, and (e) other regulatory capital constraints. The OCC and Federal Reserve also may issue additional guidance regarding implementation of the expanded authority. And many banks also maintain internal limits on product type, geographic concentration, and sponsor concentration which may limit demand further or push capital into one kind of investment or another. Each bank will want to evaluate its CRA portfolio strategy to determine whether the expanded authority should be used for additional LIHTC investments, NMTC tax credit investments, community development financial institution investments, community development funds, or other qualifying public welfare investments.

Larger institutions generally already maintain dedicated community development investment teams and may be well positioned to deploy the additional capacity. Regional and community banks may have sufficient capital and tax appetite, but may not have the operational capacity to underwrite and monitor additional tax credit investments. This may create opportunities for syndicators and fund sponsors to develop additional CRA-related investment products tailored to smaller bank investors that do not require as much internal bandwidth as certain types of tax credit investments.

Key Takeaways

- Institutions approaching the previous 15% cap may now have meaningful additional capacity for LIHTC and other qualifying community development investments.
- The amendment removes one regulatory constraint on bank investment, but institutions will continue to evaluate opportunities based on tax appetite, CRA objectives, pricing, portfolio diversification, and internal concentration limits.
- Syndicators and fund sponsors may benefit from expanded bank investment capacity, particularly as additional LIHTC equity is needed to support recently enacted federal housing tax incentives.
- Whether the expanded authority ultimately increases LIHTC pricing or investment volume remains to be seen and will likely depend on broader market conditions and individual investor strategies.

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