Should your Bank Consider becoming a Community Development Financial Institution (CDFI)?

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Specific Benefits to Banks of CDFI Designation

CDFI Banks receive 2 big benefits

- CDFI Banks are exempt from the:
  - Ability to Repay Rule
  - Qualified Mortgage Requirements
- Intangible Benefits:
  - Are regulators more trusting/forgiving of a bank with a mission of promoting community development?

CDFI Award Programs

Numerous Benefits

- Technical Assistance Awards
- Financial Assistance Awards
- Bank Enterprise Awards
- CDFI Bond Guarantee Program
- New Market Tax Credits Program
- Emergency Capital Investment Program
- CDFI Rapid Response Program

Technical Assistance Awards

- Awarded to allow existing CDFIs and certifiable CDFIs to build organizational capacity to provide affordable financial products and services.
  - Grants can be used for numerous purposes, including to:
    - purchase equipment,
    - hire consulting or contracting services,
    - pay salaries and benefits, or
    - train staff or board members.

Technical Assistance Statistics

- Total number of awards - 127
- Total amount awarded - $15.8 million
- Type of organizations receiving awards
  - Loan Funds - 70
  - Credit Unions - 53
  - Banks/Bank Holding Companies - 3
  - Venture Capital - 1

Financial Assistance Awards

- Base Financial Assistance awards of up to $1 million allow CDFIs to sustain and expand their financial products and services.
  - CDFIs must match this award with funds from a non-federal source.
  - Financial assistance awards awards can be used for:
    - lending capital, loan loss reserves, capital reserves, financial services, and development services to achieve at least one of the following FA objectives:
      - Increase volume of products or services
      - Provide new products or services
      - Expand operations into new geographic areas
      - Service new targeted populations
- Other types of financial assistance awards include:
  - Persistent Poverty Counties Financial Assistance (PPC-FA),
  - Disability Funds-Financial Assistance (DF-FA), and
  - Healthy Food Financing Initiative-Financial Assistance (HFFI-FA) awards

2020 Financial Awards Statistics

- 230 CDFIs received awards
- Total amount awarded - $127.0 million
- Type of organizations receiving awards
  - Loan Funds - 137
  - Credit Unions - 55
  - Banks/Bank Holding Companies - 33
  - Venture Capital Funds - 5

Bank Enterprise Awards

- Awards given to FDIC-insured depository institutions for making investments in the most economically distressed communities in the nation.
  - The BEA Program provides monetary awards to banks and thrifts that have successfully demonstrated an increase in their investments in census tracts with at least 30% of residents having incomes less than the national poverty level and 1.5 times the national unemployment rate. The awards also help banks and thrifts offset some of their risk and meet capital ratio requirements.
- Qualifying Activities:
  - CDFI Financing and Investments
  - • Consumer and Commercial Financing
- In 2020, the BEA program awarded more than $25.2 million to organizations.

CDFI Bond Guarantee Program

- CDFIs can apply to the CDFI Fund for authorization to issue bonds worth a minimum of $100 million in total.
  - The Secretary of the Treasury provides a 100 percent guarantee on these loans, with a maximum maturity of 30 years.
  - The Qualified Issuer sells the government-backed bonds to the Federal Financing Bank (FFB)—a government corporation that ensures the efficient use of federal financing—and bond proceeds are used to extend credit to CDFIs for community development purposes.
    - The Qualified Issuer thus acts as a "go between" financier to the broader CDFI community.
- This provides long-term credit at below-market rates.

New Market Tax Credits Program

- The new markets tax credit (“NMTC”) program was enacted as part of an overall appropriations bill (Omnibus H.R. 4577) in 2000. The NMTC Program is governed by Sec. 45D of the Code.
- The NMTC is a 39% federal tax credit available to investors over a period of seven years equal to 5% of the qualified equity investment or “QEI” for the first three years and 6% of the QEI for the remaining four years.

New Market Tax Credits Program

- The Investor becomes entitled to claim the NMTCs after it makes an investment of cash into a community development entity (a "CDE").
- The CDE takes the QEI and makes qualified low-income community investments ("QLICIs") to a qualified active low-income business (a "QALICB") in exchange for certain fees.
- The initial investment of cash in the CDE generates the NMTCs for the Investor and not the subsequent use of the QEI to make the QLICIs.
- An organization that is currently certified as a CDFI by the CDFI Fund or designated as a Specialized Small Business Investment Company (SSBIC) by the Small Business Administration automatically qualifies as a CDE and may apply to receive an NMTC allocation.

Emergency Capital Investment Program

- Established by the Consolidated Appropriations Act, 2021 and created to encourage low- and moderate-income community financial institutions to increase their efforts to support small businesses and consumers in their communities.
- Treasury will provide up to $9 billion in capital directly to (CDFIs) or minority depository institutions (MDIs) to, among other things, provide loans, grants, and forbearance for small businesses, minority-owned businesses, and consumers, especially in low-income and underserved communities, that may be disproportionately impacted by the economic effects of the COVID-19 pandemic.
- Treasury set aside $2 billion for CDFIs and MDIs with less than $500 million in assets and an additional $2 billion for CDFIs and MDIs with less than $2 billion in assets.
- Applications must be submitted by May 7, 2021.

CDFI Rapid Response Program

- The 2021 COVID Act provided $1.25 billion to the CDFI Fund to award CDFIs with grants to deliver immediate assistance in communities impacted by the COVID-19 pandemic.
    - This process will be completed by the time any new bank could become a CDFI but is a good example of the types of benefits that can arise for CDFIs.

CDFI Eligibility Requirements

What is a CDFI?

- "an entity currently meeting the requirements described in § 1805.201."
- Under Section 1805.201 of the U.S. Banking Regulations, an applicant entity must demonstrate to the CDFI Fund that it satisfies six criteria prior to being certified as a CDFI:
    1. meet the primary mission test
    2. be a financing entity
    3. serve a target market
    4. provide development services
    5. meet the accountability requirement, and
    6. not be a government entity. See 12 C.F.R. § 1805.104.

Primary Mission Test

"A CDFI must have a primary mission of promoting community development."

- CDFI Fund will consider
  - whether the "activities of the entity are purposefully directed toward improving the social and/or economic conditions of
    - underserved people (including Low–Income persons or persons who lack adequate access to capital and/or Financial Services); and/or
    - residents of economically distressed communities (which may include Investment Areas)

Financing Entity

- A CDFI must be a “financing entity”
  - predominant business activity is the provision, in arms-length transactions, of Financial Products and/or Financial Services
  - Includes:
    - a depository institution holding company;
    - an insured depository institution, insured credit union, or state-insured credit union; or
    - an entity that has such a “predominant business activity” based on an analysis of its financing statements, organizing documents, and any other information required to be submitted as part of its application

Target Market: Investment Areas

- A CDFI must serve a target market. An entity demonstrates that it meets this requirement by demonstrating that it provides Financial Products and/or Financing Services in “Investment Areas” and/or to “Targeted Populations”.
- Investment Areas
  - Area located in the U.S. or its territories
  - Area of “economic distress” with “significant unmet needs for loans, Equity Investments, Financial Products or Financial Services.”
  - Area that encompasses or is wholly located within an Empowerment Zone or Enterprise Community

Target Market: Investment Areas

- An area meets the "economic distress" definition if:
  1. The percentage of the population living in poverty is at least 20 percent;
  2. In the case of an Investment Area located:
     i. Within a Metropolitan Area, the median family income shall be at or below 80 percent of the Metropolitan Area median family income or the national Metropolitan Area median family income, whichever is greater; or
     ii. Outside of a Metropolitan Area, the median family income shall be at or below 80 percent of the statewide non–Metropolitan Area median family income or the national non–Metropolitan Area median family income, whichever is greater;
  3. The unemployment rate is at least 1.5 times the national average;
  4. In counties located outside of a Metropolitan Area, the county population loss during the period between the most recent decennial census and the previous decennial census is at least 10 percent; or
  5. In counties located outside of a Metropolitan Area, the county net migration loss during the five-year period preceding the most recent decennial census is at least five percent.

Target Market: Targeted Population

- An entity that directly or indirectly targets "individuals, or an identifiable group of individuals, who are Low-Income persons or lack adequate access to Financial Products or Financial Services in the entity's Target Market
- These persons must be located in the United States or its territories.
- Low-Income is defined to mean:
    - income, adjusted for family size, of not more than:
        - (1) For Metropolitan Areas, 80 percent of the area median family income; and
        - (2) For non–Metropolitan Areas, the greater of:
            - (i) 80 percent of the area median family income; or
            - (ii) 80 percent of the statewide non–Metropolitan Area median family income.

CFDI Mapping Tool

Development Services

- A CDFI must have a track record of providing Development Services in conjunction with its Financial Products and/or Financial Services.
- Development Services is defined as:
    - activities undertaken by a CDFI, its Affiliate or contractor that promote community development and shall prepare or assist current or potential borrowers or investees to use the CDFI’s Financial Products or Financial Services. For example, such activities include, financial or credit counseling; homeownership counseling; and business planning and management assistance

Accountability

- Accountability to the Target Market is the fifth requirement. “A CDFI must maintain accountability to residents of its Investment Area(s) or Targeted Population(s) through representation on its governing board and/or advisory board(s).

Partnering with CDFIs

Bank/CDFI Partnerships

- Banks may partner with CDFIs to create new programs through a joint venture or other partnerships.
- Banks can provide an alternative lending platform through partnerships with CDFIs to serve targeted populations.
- Bank may earn CRA credit with investments in CDFIs
- May help customers become loan ready by offering CDFI wrap around services

Nelson Mullins Team

Thank you for joining us today and please reach out for assistance in structuring your CDFI or other Bank/Bank Partnership transactions.

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