Testimony of John Holdsclaw IV, Executive Vice President, National Cooperative Bank and President, CDFI Coalition before the Subcommittee on Housing and Community Development of the Senate Committee on Banking, Housing, and Urban Affairs

Exploring How Community Development Financial Institutions Support Underserved Communities

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My name is John Holdsclaw, IV, President of the CDFI Coalition, and I am the Executive Vice President of Strategic Initiatives at the National Cooperative Bank, a leading financial institution dedicated to providing banking solutions to cooperatives, their members, and socially responsible organizations nationwide. Thank you for this opportunity to testify on the Community Development Financial Institutions Fund (CDFI) Fund and the success of CDFIs in delivering financial services to underserved low-income urban, rural, and tribal communities.

About the CDFI Coalition

The CDFI Coalition was formed in 1992 by a variety of nonprofit organizations and activists concerned about the persistent and pervasive lack of financing capital available in distressed urban neighborhoods and poor rural communities. Our Coalition is made up of more than 150 organizations—including loan funds, community development banks, community development corporations, venture funds, microlenders, Native American organizations, and credit unions—that are working to finance affordable housing, small businesses, and community facilities at the ground level.

About the CDFI Fund

The Community Development Financial Institutions (CDFI) Fund was established within the Department of Treasury in the Riegle Community Development and Regulatory Improvement Act (PL 103-325) of 1994. The purpose of the agency is to "promote economic revitalization and community development through investment in and assistance to community development financial institutions, including enhancing the liquidity of community development financial institutions."

The CDFI Fund administers the following core programs, and each program awards funds annually through an independent and competitive application process, including the *Financial Assistance (FA), Technical Assistance (TA) Awards, The Native American CDFI Assistance (NACA) Program, The Bank Enterprise Award (BEA) Program, New Markets Tax Credit (NMTC) Program, Capital Magnet Fund, the CDFI Bond Guarantee Program, Economic Mobility Corps, and Small Dollar Loan Program*.

The Challenges Facing Low-Income Communities and Populations

Even before the pandemic, low-income communities and communities of color faced significant obstacles in accessing financial services, including mortgage, consumer, and business loans, financing for community facilities and affordable housing, and the patient, flexible capital needed to sustain a healthy economy. These are the communities CDFIs serve.

One of the biggest challenges facing underserved communities and populations is the lack of existing assets. Indigenous people and people of color, in particular, have fewer assets to use to secure loans. For example, the median net worth of white families is nearly nine times greater than black families, according to the Federal Reserve's 2019 Survey of Consumer Finances. Entrepreneurs of color are therefore less likely to self-finance a business or borrow funds from friends and family.

With fewer resources to tap into, businesses in low-income communities tend to be smaller than businesses in more prosperous communities. The average business in a low-income community has 20% fewer employees than businesses in other areas, according to a 2017 report by the Small Business Administration.

According to a working paper published in 2018 by the Richmond Federal Reserve, Black and Latino business owners are significantly more likely to be discouraged borrowers[1]. Minority borrowers face more scrutiny and receive less assistance when applying for bank loans than their white urban counterparts.

Small towns and farming communities also continue to be underserved by conventional lenders. The number of community banks in the United States has declined by an average of 300 per year over the past 30 years, according to data from the Federal Deposit Insurance Corporation. During the Great Recession, when lending plummeted nationwide, in Appalachia, lending "decreased to a greater extent, standing at 18 percent below national levels at the end of the recession…in the Region's economically distressed counties, lending was 56 percent below national levels. Further, growing disparities were found in lending to businesses with revenues of less than $1 million and in counties with limited access to non-credit-card bank lending."[2]

Residents of Indian Country also face significant challenges in securing commercial credit, including significantly longer distances from brick-and-mortar financial institutions and poor and limited internet for mobile or online banking. This is compounded by a lack of equity resources, collateral, and credit history; experiences and perceptions among Native entrepreneurs that commercial bank financing is difficult to secure; and a lack of diversity in funding sources.[3] According to an analysis of 2018 Census and Bureau of Labor data by the National Community Reinvestment Coalition, Native Communities experience the highest rates of unemployment (6.6 percent) and poverty (25.4 percent) among minority

[1] Financing Patterns and Credit Market Experiences: A Comparison by Race and Ethnicity for U.S. Employer Firms. Report by Alice Robb, Ph.D. for the Office of Advocacy, U.S. Small Business Administration, February, 2018.
[2] Access to Capital and Credit in Appalachia and the Impact of the Financial Crisis and Recession on Commercial Lending and Finance in the Region. July 2013, Josh Silver and Archana Pradhan, National Community Reinvestment Coalition; and Spencer M. Cowan, Woodstock Institute.
[3] Miriam Jorgensen and Randall K.Q. Akee. 2017. Access to Capital and Credit in Native Communities: A Data Review, digital version. Tucson, AZ: Native Nations Institute.

groups.[4] Native CDFIs are often the only resources for financial products and services in tribal communities.

A 2019 report by the Federal Reserve found that since the end of the last (great) recession, *"low-income neighborhoods have experienced larger declines in the number of banks and larger increases in the number of alternative financial services companies compared to higher-income areas."*

The COVID-19 crisis has exacerbated the already difficult situation. According to an April 2020 report by the Department of Health and Human Services,[5] residents of low-income communities are more likely to work in professions at high risk of COVID infection: as "essential workers" in public-facing retail or service sector jobs, as nurses, and as first responders. Excess deaths during the pandemic surged in low-income communities during the recent pandemic, and in particular, rural counties and tribal lands. For example, in Navajo County, AZ, more than 15 people out of 1,000 died in 2020, up more than 40% from the annual average of 11 people per 1,000[6].

After early pandemic relief funds were gobbled up by large companies in higher-income areas, Congress made an effort to ensure pandemic relief resources reached difficult to serve communities, and CDFIs were part of those successes, as I will discuss in a moment. With the Omicron outbreak underway, we must again think critically about how we can equitably direct resources to ensure recovery resources reach the areas of greatest need. CDFIs can once again play a part.

About CDFIs and Their Mission

CDFIs emerged to help address the challenges facing low-income communities and disadvantaged populations discussed earlier. They provide financial services in urban neighborhoods and rural areas underserved by traditional financial institutions, particularly those communities with high rates of poverty and unemployment. Certified CDFIs must target at least 60 percent of their financial products and services to low-income communities and populations.

The CDFI industry has grown significantly since the advent of the CDFI Fund in 1994. Today, the CDFI Fund has certified 1,298 CDFIs across the country, providing vital community development lending services in all sizes and types of communities. Certified CDFIs include 565 loan funds, 416 credit unions, 134 depository institution holding companies, 167 banks or thrifts, and 16 venture capital funds, located in rural and urban areas in all 50 states, the District of Columbia, Puerto Rico, and Guam.

By leveraging over $12 in private capital to every $1 in federal support, CDFIs are filling the critical missing lending gap encountered in many communities, creating jobs, improving housing and community facilities, building wealth, and creating economic opportunity.

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[4] Dedrick Asante Muhammad, Rogelio Tec and Kathy Ramirez, November 18, 2019. Racial Wealth Snapshot: American Indians/ Native Americans.

[5] The Impact of the First Year of the COVID-19 Pandemic and Recession on Families With Low Incomes. Amanda Benton, Erica Meade, and Alec Vandenberg for the Department of Health and Human Services. Sep 20, 2021.

[6] Amanda Montañez; Source: "County-Level Estimates of Excess Mortality Associated with COVID-19 in the United States," by Calvin A. Ackley et al. Preprint posted May 5, 2021.

Recent Impact
The CDFI Fund administers a growing portfolio of programs designed to create jobs, build affordable housing, construct and support essential community facilities, provide financial counseling, and invest in neighborhood revitalization initiatives—all in distressed and underserved communities lacking access to traditional lending or banking institutions.

The latest impact data from an independent audit by the Department of Treasury highlighted the impact of CDFI Fund programs in 2020.

- *CDFI Fund Financial Assistance Award* recipients unleashed $39 billion in loans and investments to 125,000 businesses and millions of individuals. They financed 50,000 affordable housing units and thousands of nonprofits and community facilities.

- *Healthy Foods Financing* award recipients financed 409 grocery stores, markets, and fresh food projects totaling over 4 million square feet.

- *Native Assistance Program* recipients helped Native CDFIs originate $1.6 billion in loans and investments to nearly 2,500 businesses and tens of thousands of individuals.

- *New Markets Tax Credit* allocatees made $3.3 billion in loans and investments to hundreds of projects in low-income communities, creating nearly 13,000 permanent full-time jobs and 23,000 construction jobs.

- Over the past five years, through 2020, *Capital Magnet Fund* award recipients helped secure financing commitments for tens of thousands of affordable housing units. Since 2013, the *CDFI Bond Program* has supported $1.3 billion in affordable financing for community facilities, nonprofits, commercial real estate, and other community development projects.

- CDFI Fund financial assistance helped boost the capacity of hundreds of CDFIs in 2020. *The Small-Dollar Loan Program* enabled 52 CDFIs to increase their capacity to provide fair and affordable loans in their communities and to help unbanked and underbanked borrowers build their credit. *The Economic Mobility Corps, Bank Enterprise Awards,* and *CDFI Technical Assistance* programs all helped boost CDFI capacity to serve low-income communities.

Fiscal Year (FY) 2021 was the busiest year in the history of the CDFI Fund. Altogether, the CDFI Fund provided nearly $1.5 billion in monetary awards and loans, including $1.25 billion through the CDFI Rapid Response Program and over $180 million in technical and financial assistance awards. The Fund also committed to guaranteeing $100 million in bonds and allocated $5 billion in New Markets Tax Credits.

CDFIs and Pandemic Relief

CDFIs played an essential role in helping stabilize and support vulnerable communities during the pandemic. America's low-income rural and urban communities have borne not just the health consequences but also the economic consequences of the pandemic. High unemployment rates and small business failure were primarily concentrated in the underserved communities where CDFIs work.

During this unprecedented time in history, CDFIs answered the call of marginalized communities and small businesses through participation in the Paycheck Protection Program (PPP) and delivering innovative financial products and programs to provide loans and investments; capacity building; training and technical assistance services; and promoting development services efforts that bring credit and capital to individuals and communities.

After the first round of PPP loans went overwhelmingly to sophisticated borrowers and well-connected businesses, Congress established a set-aside for future rounds for Community Financial Institutions (CFIs), which included CDFIs and other mission-based lenders. The effort succeeded. Community lenders reached underserved businesses with a much greater proportion of their PPP loans than conventional banks. According to the SBA, through May of 2021, CDFIs made 1.3 million PPP loans totaling over $30 billion or 21% of total loans. Their average loan size was $21,653 compared to $41,560 across all lender classes, and nearly 40% of their loans reached business in low- and moderate-income communities, compared to 28% across all lending sources.

Additionally, CFI loans reached more small businesses. For example, 78% of their PPP loans went to businesses requesting less than $250,000. Moreover, 15.7% of CFI-made loans were made to businesses in rural communities, closely keeping with the 16.6% of all loans (some $45.5 billion) that went to rural businesses.

The 116th Congress made a substantial investment in CDFIs. Recognizing the critical role played by CDFIs in rural and urban communities across the country, The Consolidated Appropriations Act, 2021 (PL 116-260) provided:

- $1.25 billion for CDFIs to provide technical and financial services to communities and businesses hard hit by the Coronavirus pandemic. In February, the CDFI Fund released the application for the so-called Rapid Response Program (RR), and in June 2021, it awarded grants to 850 certified CDFIs;
- $1.75 billion for CDFIs and Minority Depository Institutions (MDIs) increase lending and investing activity targeted to low-income and minority communities and populations. We hope to see more information from the CDFI Fund on this initiative soon; and
- $9 billion for the Emergency Capital Investment Program (ECIP). ECIP was designed to provide capital to depository institutions that are certified CDFI or MDIs. The Department of the Treasury opened the application process for CDFI's and MDIs in March 202i and received over 200 applications totaling more than $12 billion in requests. On December 14, Secretary Yellen and Vice President Harris announced the deployment of $8.7 billion of direct investments in banks, credit unions, and holding companies that are certified CDFIs or MDIs.

As the economy slowly improves, the small businesses that survive will have a pressing need for the patient capital, particularly working capital, to get their businesses back on their feet. CDFIs could have done more if they had the capital and if more CDFIs had been approved as PPP lenders during the early days of the program and can do more going forward.

Looking to the Future

The recent growth of the CDFI industry presents both opportunities and challenges. The federal government made an unprecedented investment into CDFIs over the past few years with the hope of further scaling the industry and expanding its impact. CDFIs' performance during the pandemic showed they have the capacity to deliver a high volume of financial products and services to communities and people outside the economic mainstream. However, Congress – and the CDFI Fund – can do more to scale the CDFI movement while ensuring that certified CDFIs maintain their role as trusted, mission-driven lenders in underserved communities.

<u>Proposals:</u>

$1 billion in annual appropriations for CDFI assistance programs through the CDFI Fund: The CDFI Coalition urges Congress to invest more in CDFIs by increasing the annual authorization to $1 billion for the CDFI Fund.

The CDFI Coalition projects the following outcomes from $1 billion in annual appropriations for the CDFI Fund:

- $12 billion in total investment in low-income communities, over 100,000 affordable housing units created or preserved, thousands of loans and investments in childcare centers, health clinics, and community facilities, nearly two million consumer and homeownership loans, and hundreds of thousands of loans and investments in businesses in target markets.

Strengthen the Bond Guarantee Program (BGP): Despite the unique benefits of the BGP, the program has not realized its full potential. Only 26 CDFIs have participated in the bond program and as Qualified Issuers, and many CDFIs, particularly smaller organizations, are not able to access this valuable source of long-term, fixed-rate financing. The CDFI Coalition agrees with CRF, USA's recommendations on strengthening the program by (1) reducing the minimum bond issuance from $100 million to $25 million and (2) increasing program efficiency and consistency by granting the BGP permanent authority.

Build the administrative capacity of the CDFI Fund: To sustain the recent momentum and growth in the CDFI industry, Congress should support efforts to build the administrative capacity of the CDFI Fund. The previous administration proposed four consecutive budgets aimed at dismantling the Fund. The agency needs more resources to administer a growing portfolio of financial assistance awards, bonds, and tax credit. The CDFI Fund needs more people and an investment in systems to administer its programs and authorities, to say nothing of compliance monitoring and providing technical assistance.

Seek additional CDFI feedback on the certification process: With the additional administrative resources, the CDFI Fund can refocus on overhauling the certification process. The Fund released its draft certification rule for public comment in 2019 but delayed implementation of the rule due to the pandemic. The pandemic has drastically altered the situation in CDFIs' target markets.

Since 2019, the CDFI industry has grown significantly in size and scope. Before proceeding with the certification rule crafted in 2019, the Coalition urges the CDFI Fund to convene stakeholder meetings with the CDFI industry. Many CDFIs – including CDFI loan funds – have used additional resources to expand their service areas. The certification rule proposed in 2019 may make it difficult for many established CDFIs to scale and serve more markets. This is particularly the case for CDFIs with a multi-state footprint.

The certification rule must also ensure CDFIs maintain their high standards for thoughtful lending and investment in their target markets. With more resources, the CDFI Fund can continue to monitor the performance of the expanding CDFI investment footprint and ensure that new entrants to the industry are providing affordable financial products and services in underserved communities.

Update the Community Reinvestment Act: The Community Reinvestment Act has been a powerful tool in delivering financial services to historically disadvantaged populations. CDFIs rely on CRA to secure capital from private financial institutions, a key source of capital. Without CRA, today's CDFI industry would be a fraction of its current size and the scale of its lending and impact correspondingly reduced. Communities count on CDFIs, and CDFIs depend on CRA to secure capital.

The Coalition was pleased that the Office of the Comptroller of the Currency withdrew the final rule for its misguided 2020 CRA overhaul earlier this year. We are encouraged by the willingness of the three regulatory agencies to work together on a CRA unified framework.

While CRA has been generally successful, it is in need of an update and a tune-up. To meet CRA's requirements, banks invest in affordable housing, small businesses, and other community development activities that bring historically disadvantaged populations into the economic mainstream. However, as the recent pandemic and the protests of the summer of 2020 made clear, the legacy of discriminatory red-lining lives on in many communities of color where poverty and unemployment still outpace the national average and community infrastructure is inadequate. With the right data-driven reforms, CRA can be much more effective in delivering on its original promise for these communities.

At a baseline, CRA modernization should result in a net increase in both the quantity and quality of financial products and services available in LMI areas. The burden is on federal regulators to show – with data and evidence – that their reform proposals can meet those baseline goals for reform.

The Coalition believes a modernized CRA framework should meet the following five tests. Reforms should: (1) boost the voices and input of community groups in conducting CRA exams and developing CRA ratings; (2) generate additional investment in traditional community development activities in CRA deserts; (3) encourage thoughtful, high-impact investments significant benefits to low- to moderate-income (LMI) communities; (4) strengthen accountability for financial institutions; and (5) most importantly, ensure financial institutions are serving people of color and traditionally disadvantaged groups.

Conclusion

The last Congress made a substantial bet on CDFIs as a conduit for delivering relief and revitalization to our hardest-hit communities and populations. Thus far, the bet has paid off. The CDFI industry is growing, serving more businesses and families, and delivering financial services to areas of persistent poverty and unemployment. Providing more resources through the CDFI Fund will ensure the continued growth of mission-driven financial services.

Thank you for this opportunity to testify. I would be happy to respond to any questions.