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POLICY BRIEF: MAINTAINING STRONG SUPPORT FOR COMMUNITY DEVELOPMENT FINANCIAL INSTITUTIONS (CDFIs)

SUMMARY OF RECOMMENDATIONS:

Legislative

- Appropriations:
  - Preserve annual appropriations for the U.S. Treasury Department's Community Development Financial Institutions (CDFI) Fund at not less than the $354 million Senate Appropriations Committee proposal for FY 2025 and FY 2026 [Chart 2].
- Tax:
  - Permanently extend the New Markets Tax Credits (NMTC) and give priority to applicants that are CDFIs.
  - Enact the Wicker-Warner Community Development Investment Tax Credit Act (S.2963) as part of anticipated tax legislation.
- Banking:
  - Enact the Crapo-Warner Scaling Community Lenders Act (S.1442) as part of any banking or housing legislation.

Regulatory

- US Treasury Department:
  - CDFI Fund: Amend new CDFI certification policy to ensure rural organizations retain certification.
  - ECIP: Focus on effective implementation of the Emergency Capital Investment Program (ECIP), with an approach to the disposition of ECIP capital that provides options to all types and sizes of participants and ensures funds remain in the communities they were originally directed to support.
- Bank Regulatory Agencies:
  - Expeditiously enact provisions of new Community Reinvestment Act (CRA) regulations that support and promote CDFIs. If amendments are made to the current proposed rule, the pro-CDFI provisions should be retained.
- Consumer Financial Protection Bureau:
  - ECOA: Amend Equal Credit Opportunity Act (ECOA) rules to give CDFIs and Minority Depository Institutions (MDIs) the option to collect borrower demographic data.

BACKGROUND:

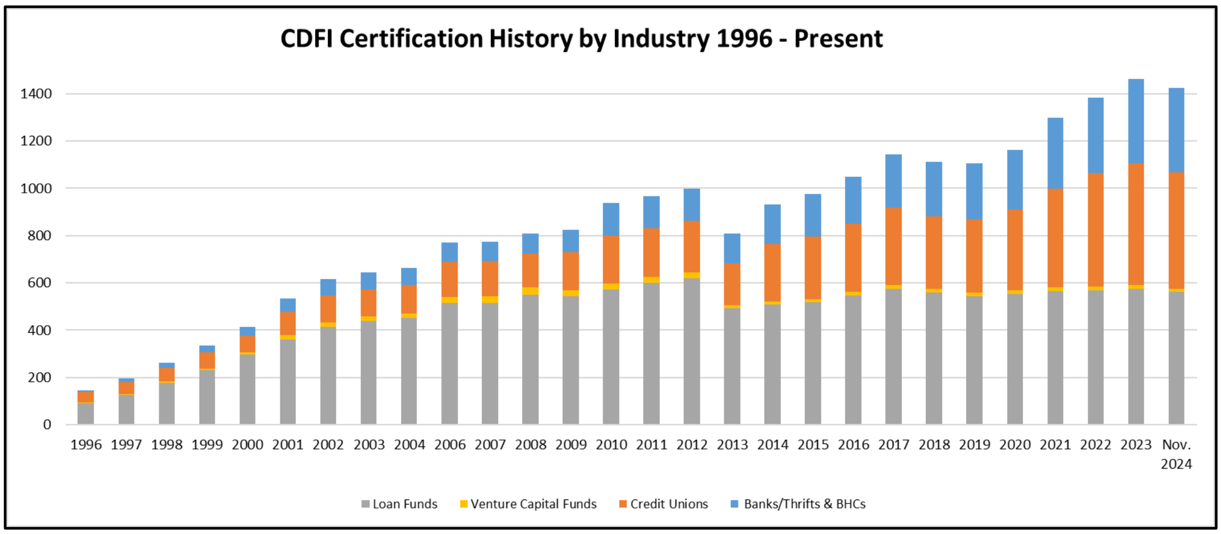
CDFIs DEFINED

CDFIs and the CDFI Fund align squarely with conservative free market priorities. CDFIs are market-based financial institutions that let businesses and individuals get the most out of the opportunities they seize. CDFIs emphasize the importance of economic opportunity and growth by investing in people and places hard hit by long- and short-term economic disruption. CDFIs measure success by focusing on the "double bottom line" of financial performance and promoting impact. By leveraging a small amount of federal dollars from the CDFI Fund, CDFIs extend a "hand up," providing much-needed financial services that help create jobs, promote small business growth, build affordable housing, and revitalize communities. Further, regulated CDFIs offer retail financial services to un- and underbanked customers. To certify as a CDFI, a financial institution must direct at least 60% of their lending toward economically distressed people and communities.

CDFIs include a diverse group of financial intermediaries including regulated banks and credit unions and nonregulated loan funds and venture capital funds. As of November 2024, per the CDFI Fund, there are 1,425 certified CDFIs including: 356 banks and bank holding companies (25%), 494 credit unions (35%), 561 loan funds (39%) and 14 venture capital funds (1%).

Without CDFI banks in particular, many rural and small communities would lack adequate access to financial services and investment, which stymies growth and perpetuates poverty.

Chart 1: CDFI Certification History



Per a 2023 analysis by the New York Federal Reserve Bank, total assets in the CDFI industry tripled to more than $450 billion between 2018 and 2023. Using 2023 data from the FDIC, NCUA and CDFI Fund, the approximate break down of the industry by total assets is 28% banks and bank holding companies, 63% credit unions, 8% loan funds, and less than 1% for venture funds.

CDFI banks are an important subsector of CDFIs and a niche within the banking industry, comprising 4.3% of the entire banking sector by number of institutions. CDFI banks provide access to credit and financial services in communities that are not adequately served by traditional banks. All CDFI banks are privately owned, federally insured depository institutions with a primary mission of promoting community development to ensure economic vitality and opportunity. There are 196 CDFI banks and 160 bank holding companies with the CDFI designation. CDFI banks provide financial products and services via 1,415 branches across 35 states. While banks represent 25% of the CDFI sector, they are among the fastest growing groups of CDFIs particularly in rural communities. The states with the largest concentrations of CDFI banks are Mississippi (49), Louisiana (40), Arkansas (19), Alabama (16), and Tennessee (12). Further, the states of Missouri (8), West Virginia (5), Georgia (5) and Texas (5), have seen increased bank certification over the past five years.

HOW THE FEDERAL GOVERNMENT WORKS WITH CDFIs

Federal support for the CDFI sector began in 1994 with enactment of the bipartisan Riegle Community Development and Regulatory Improvement Act of 1994. The CDFI Fund was created to promote access to credit and financial services in traditionally underserved urban, rural and Native American communities. Over 30 years, the CDFI Fund has distributed $7.6 billion in appropriated funding to CDFIs. This investment has grown the number of CDFIs from less than 200 to 1,425 institutions and leveraged billions in private resources. This investment has enabled CDFIs to reach more and more distressed rural, urban and Native American communities. CDFIs now operate broadly across the country, with a strong majority physically located in Republican-held Congressional Districts and States.

- CDFIs now have a physical location via 5,872 headquarters and/or have branch locations *in every state and territory in the nation*.
- Of the 435 Congressional Districts with voting members in them, 402, or 92% of total voting-member districts, have at least one CDFI physically located within their boundaries. Within these 402 districts:
    - 203 (50.5%) are Republican–held Congressional Districts, while 198 (49.5%) are Democrat-held Congressional Districts.[1]
    - Fully 60.6% of CDFI locations sit in Congressional Districts held by Republicans and 54.5% sit in States with two Republican senators.
    - 127 CDFI locations are in the US territories of Puerto Rico and Guam, and Washington, DC.

The CDFI Fund invests in CDFIs and their communities through a series of grant programs that are appropriated by Congress (described below). The Fund also administers the New Market Tax Credit Program (funded via the tax code) and the Capital Magnet Fund (funded from assessments on the housing GSEs).

CDFIs use a small amount of public appropriated dollars to leverage a multiple of private dollars to promote market-based activities in LMI communities. Since 1994, CDFIs have leveraged at least $8 in private sector investment for every $1 in public funding received; amounts leveraged are estimated at $60.8 billion in grants, deposits, debt, and other resources. This capital, in turn, has enabled CDFIs to makes billions in loans and investments in small businesses and homeowners, created jobs, and restore and promote economic vitality and self-sufficiency in distressed, low-income, and persistent poverty communities across the nation. In FY 2023 alone, the CDFI Fund's "flagship" CDFI Program awardees made more than 2 million loans or investments totaling more than $57 billion. This financing included $20.2 billion for consumer loans, $14.1 billion for home improvement and purchase loans, $9.8 billion for small business loans, and $5.8 billion for residential real estate transactions. CDFIs also financed nearly 77,000 affordable housing units.

CDFIs AND THE FIRST TRUMP ADMINISTRATION

During the first Trump Administration, the White House forged highly effective partnerships with CDFIs. During the first weeks of the Paycheck Protection Program (PPP), CDFI banks were among "financial first responders" outpacing "large non-community" banks in responding to local demand, reaching very small and hard-to-reach businesses, and especially meeting the needs of non-metro areas.[2] As researchers

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[1] Based on analysis of 118th Congress using PolicyMap (policymap.com). Data on boundaries of Congressional Districts to be posted in Q1 2025, but expected to yield similar results.

[2] Allen, K. and Whitledge, M., "Further evidence on the effectiveness of community banks in the Paycheck Protection Program," June 2022

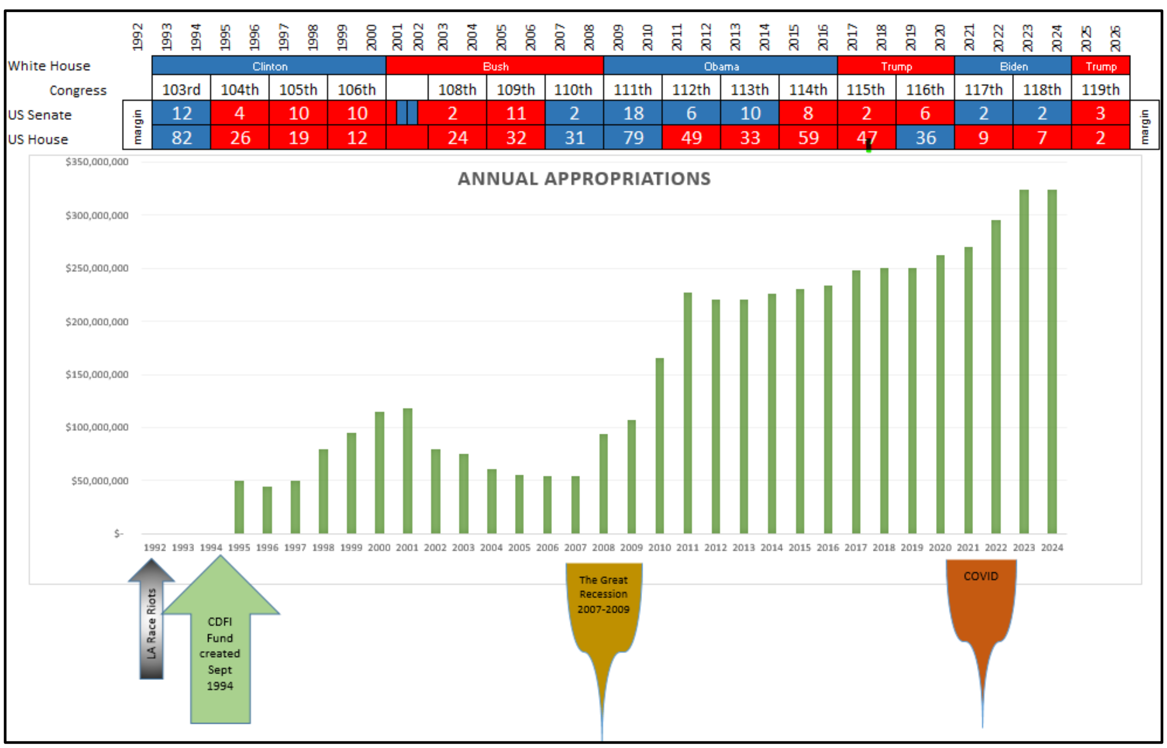
noted, this success continued through all rounds of the program and was tightly correlated to the banks' "closely held ownership coupled with service-oriented missions, relational banking practices, and community ties (which) leave alternatives like community banks or CDFIs less exposed to shareholder pressures for short-term profit and *less prone to abandon communities to invest elsewhere*."[3] (Emphasis added). According to Small Business Administration (SBA) data, CDFIs and other mission lenders, known as Community Financial Institutions (CFIs), made 1.38 million PPP loans totaling approximately $30 billion, twice the statutory set-aside. The average size of CFI loans was $21,650, compared to $41,560 for all lenders. SBA reported that over 77% of CFI loans were less than $150,000; almost 40% were provided to low-moderate income communities, and 15.7% to rural areas.

Later in 2020, the Trump administration worked with Congress to include an unprecedented $12 billion of anti-recession funding for CDFIs in the Consolidated Appropriations Act of 2021. This Act included $9 billion in long-term capital for depository CDFI banks and credit unions through the Emergency Capital Investment Program (ECIP), which unlocked access to capital for the hardest-to-serve small businesses, provided mortgages to underserved homebuyers, and other market needs. ECIP participants made more than $58.3 billion in loans over 18 months, including $10.3 billion in rural communities and $10.2 billion in persistent poverty communities. The Act also provided $3 billion in grant monies via the CDFI Fund to empower CDFIs to promote economic recovery in communities hardest hit by COVID.

BIPARTISAN CDFIs ARE A PROVEN MARKET BASED SOLUTION FOR ECONOMIC GROWTH

CDFIs have earned bipartisan support as one of the federal government's best market-based strategies for creating economic opportunity. As CDFIs have grown in numbers and reach, their bipartisan support has grown as demonstrated in Chart 2. To note, half of the 26 members of the Senate CDFI Caucus are Republicans and half are Democrats.

Chart 2: CDFI Fund Appropriations History & Executive and Legislative Branch Changes



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[3] Casell, M., Schwan, M., and Schneiberg, M., "Bank Types, Inclusivity, and Payroll Protection Program Lending During COVID-19," March 2023

POLICY RECOMMENDATIONS

LEGISLATIVE

Appropriations: Preserve annual appropriations for the CDFI Fund at not less than the $354 million Senate Appropriations Committee proposal for FY 2025 and FY 2026.

Chart 3: CDFI Fund Appropriations History

Treasury Programs $ in millions	FY23 Final	FY24 Final	FY25 Budget	House Committee	Senate Committee
CDFI Fund	$324	$324	$324.90	$276.60	$354
CDFI FA/TA Grant Programs	196	188	210	170	191
Native Initiative	25	28	25	35	35
Healthy Food Financing Initiative	24	24	0	0	24
Bank Enterprise Award	35	40	35	35	40
Admin and Research	35	35	35.9	33.6	45
Disabilities Fund*	10	10	10	10	10
Small Dollar Loan Fund	9	9	9	3	9
Economic Mobility Corps*	2	2	0	0	2
Bond Program subsidy	0	0	10	0	10
Bond Guarantee program authority	500	500	500	500	500

**set aside from TA/TA*

The appropriated CDFI Fund programs that support CDFIs include:

CDFI Program: This flagship program provides Financial Assistance (FA) and Technical Assistance (TA) grants to enable CDFIs to expand lending, launch new products, and serve new markets. This program requires $1 in private matching funds for each $1 of Federal funds. Within the program, awards are also set aside for CDFIs that expand healthy food financing, and that specifically serve individuals with disabilities.

Bank Enterprise Award (BEA) Program: The BEA program awards grants to FDIC-insured depository institutions for increasing loans and investments in the most economically distressed communities. BEA focuses on communities with high poverty and unemployment rates, and principally benefits very small CDFI and community banks.

Small Dollar Loan Program (SDLP): The SDLP provides grants for Loan Loss Reserves and Technical Assistance to enable CDFIs to establish and maintain small dollar loan programs. These grants help unbanked and underbanked populations build credit, access affordable capital, and improve access into the mainstream financial system.

Native Initiatives: This program supports the creation and expansion of Native CDFIs. Native CDFIs help Native Communities thrive by increasing their access to credit, capital, and financial services. The program uses a combination of financial, technical assistance, and training to build CDFI capacity.

CDFI Bond Guarantee Program: The Bond Guarantee Program responds to a critical market need for long-term, low-cost capital that can spur economic growth. Although funded through appropriations, the CDFI Bond Guarantee Program does not offer grants, but is instead a federal credit subsidy program: bond proceeds are debt instruments that must be repaid.

Tax Provisions

New Markets Tax Credit Extension Act (S.234 / H.R. 2539): This popular and impactful tax credit needs to be permanent. The NMTC attracts private capital into low-income communities by permitting individual and corporate investors to receive a tax credit against their federal income tax in exchange for making equity investments in specialized financial intermediaries called Community Development Entities (CDEs). The NMTC expires on December 31, 2025. The New Markets Tax Credit Extension Act of 2023 would extend the NMTC indefinitely, and should be supported, with changes. Specifically, since its establishment, the Program has been significantly oversubscribed. CDFIs have proven to be highly effective in deploying credits. Unfortunately, according to the CDFI Fund's CY 2022 award book, only 36% of allocatees are certified CDFIs. The NMTC should be amended to give priority to applicants that are CDFIs.

Community Development Investment Tax Credit Act (S.2963): New legislation can help drive private investment to CDFIs. CDFIs require equity to support their organization and lending activities. However, equity is the hardest form of capital for CDFIs to raise. To leverage private sector funding for high-impact investments, Senators Wicker and Warner have proposed a CDFI Investment Tax Credit, to provide a credit for investors making equity investments or providing other forms of long-term patient capital to CDFIs (i.e., loans with a minimum term of at least 10 years). Introduced in 2023, the bill would provide a 3% credit for the first 10 years of a qualified investment in a CDFI, 4% for the following years, up to a maximum of 10 years, with a 1% increase in the credit for investments without term or duration. The bill currently has the support of ten (5R – 5D) cosponsors

Banking

Scaling Community Lenders Act (S. 1442): New legislation can unlock balance sheet liquidity for CDFIs. Access to liquidity is an important tool for community development lenders to manage their portfolios and balance sheets, which in turn gives them more capacity to serve their communities. Introduced in 2023, Senators Crapo and Warner propose activating an existing statutory authority to allow the CDFI Fund to provide funds for loan guarantees, loan loss reserves, or other forms of credit to promote liquidity. This would support private lenders in managing risk, complying with lending limits, and diversifying their portfolios. The bill currently has the support of six (3R – 3D) cosponsors.

<u>REGULATORY</u>

CDFI Certification: CDFI certification updates require revisions to ensure rural communities benefit from the program. On December 7, 2023, the CDFI Fund published a revised CDFI Certification Application. The 2023 Application included some important, positive changes that addressed industry and community concerns submitted in response to a 2022 draft. However, several provisions still require adjustments, including those that affect the ability of many (particularly rural), CDFIs to serve their communities. We urge the Administration to ensure CDFIs of all types and in all markets receive fair treatment based on their market and business model, and that CDFIs have sufficient time to adjust practices when required by new policies.

Emergency Capital Investment Program (ECIP): The importance of equity capital to CDFIs has already been noted above. The first Trump administration's successful 2020 negotiation of ECIP directed $9 billion of equity and subordinated debt to help CDFI and MDI banks and credit unions increase lending and investments in low- and moderate-income, rural and minority communities. The program has been successful at increasing lending in these underserved geographies and to the hardest-to-serve very small businesses: Per Treasury, "From the summer of 2022 through December 2023, ECIP participants reported total originations of approximately $58.3 billion. Approximately 74%, or $43.0 billion, of these originations was Qualified Lending. Approximately 35% of these originations, or $20.6 billion, was Deep Impact Lending to the most underserved borrowers."[4] With funding deployed almost 3 years ago, lenders are now looking to the future, and we urge the incoming Administration to focus on a uniform approach to the disposition of ECIP capital that provides options for all types and sizes of institutions to access early disposition while ensuring participates remain focused on serving the communities intended to be served.

Community Reinvestment Act (CRA): Recent CRA reform included valuable improvements that should be retained**.** The CRA establishes that banks must "help meet the credit needs of the local communities in which they are chartered." A 2023 joint-agency "final rule" intended to improve the implementation of the CRA. Among several valuable provisions, the rule explicitly confers automatic CRA credit for activities in support of, and undertaken with CDFIs, regardless of their geographic proximity to the bank requesting credit. These provisions were publicly supported by national banking trades and promise to bring much needed investment into rural and small town communities. These provisions should be retained in future implementation, pending the outcome of a lawsuit filed in the Northern District of Texas.

Equal Credit Opportunity Act (ECOA): CDBA strongly supports ECOA, but we believe targeted regulatory amendments could improve its ability to promote access to capital among underserved borrowers. ECOA aims to ensure that credit is available to all creditworthy applicants without discrimination. In practice however, the rule impedes the flow of capital by prohibiting regulated CDFIs from collecting customer demographic information even for activities focused on improving, rather than restricting, access to credit. The Administration should amend ECOA rules and examination practices to give regulated CDFIs and Minority Depository Institutions (MDIs) the option to collect borrower demographic data, ideally through an exception under the Special Purpose Credit Program rules (12 CFR Part 1002).

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[4] Emergency Capital Investment Program, "2023 Investing for Impact Report," July 12, 2024, https://home.treasury.gov/policy-issues/coronavirus/assistance-for-small-businesses/emergency-capital-investment-program