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Capital for Communities – Opportunities for People℠

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Community Development Financial Institutions Fund
U.S. Department of the Treasury
601 Thirteenth Street, NW., Suite 200 South
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ATTN: Request for Public Comment on the CDFI Bond Guarantee Program

Dear Ms. Harris:

On behalf of Community Reinvestment Fund, USA, ("CRF"), I appreciate this opportunity to comment on regulations to implement the new Community Development Financial Institutions ("CDFI") Bond Guarantee Program ("CBGP" or the "Program") created by the Small Business Jobs Act of 2010. Our comments address questions included in the CDFI Fund's Request for Public Comment published in the *Federal Register* on July 1, 2011.

CRF participated in a number of the industry sponsored discussions about this new Program, chairing committees convened by the Financial Innovations Roundtable and the Opportunity Finance Network, ("OFN"). Through these efforts we shared our expertise and helped to shape industry positions on a number of key issues. While we have signed the comment letter submitted by OFN, in this letter we note those issues where we concur with the industry position and provide more specific commentary on those areas where we differ with our colleagues.

<u>BACKGROUND</u>

CRF is a national CDFI and the nation's leader in channeling resources from the capital markets to support community development financing activities. Our mission is to transform the community development finance system by accessing capital markets on behalf of local lending organizations so that together we can create long-term sustainable jobs, finance the businesses that generate jobs, and strengthen the social ecosystem that supports them – particularly in low-income communities. We operate a secondary market for community development loans, which we purchase from private nonprofits, such as CDFIs, governmental and quasi-public lending agencies. We pool these loan obligations and transform them into securities that are sold to banks, thrifts, insurance companies, pension funds and other qualified institutional investors.

Through our secondary market activities, CRF pioneered the development of asset-backed community development securities to help CDFIs and other community-based lenders access capital markets resources. We have issued nineteen series of Community Reinvestment Fund Revenue Notes totaling $325.3 million and three securities backed by affordable housing loans. In 2004, CRF marked a major milestone by issuing two rated debt offerings. One was secured by a pool of affordable housing loans totaling $84.7 million with the highest class of certificates in this offering receiving a "AAA" rating from Standard & Poor's. The second offering was collateralized by small business loans totaling $51 million - including $46 million in asset-backed securities, of which 57% received a "AAA" rating from Standard & Poor's. Since then, CRF has issued two more rated debt offerings that brought more than $100 million in capital primarily to low-income communities.

CRF was also instrumental in creating the New Market Tax Credit ("NMTC") Program and developing loan products that deliver the benefits of this tax credit to operating businesses. Together with its affiliate, National New Markets Tax Credit Fund, Inc., ("NNMTCF"), CRF has become one of the largest allocatees in the country, receiving tax credit allocations of $674.5 million and investing $52.5 million on behalf of other allocatees. These resources have been used to make flexible loans for small and medium-sized business and nonprofit borrowers located in low-income communities throughout the country. To date, we have funded 370 NMTC loans totaling $679.4 million in 187 cities in 34 states.

Overall, CRF and its affiliates have delivered nearly $1.3 billion in capital - primarily to small businesses - located in more than 750 communities across the country. This lending has, in turn, leveraged $1.3 billion in additional funds for total project resources. In partnership with 157 local lending partners, we have funded 2,310 loans in 46 states and the District of Columbia. Working through its local lending partners, CRF has directly assisted more than 500,000 people, including financing 17,465 homes of which 17,138 are affordable, financing 1,300 small businesses, creating or retaining almost 44,000 jobs and funding community facilities that serve 426,000 people.

GENERAL COMMENTS

Before addressing specific issues raised in the request for comment, we wish to make a number of general comments related to this new Bond Guarantee Program.

We *strongly commend the CDFI Fund for its efforts to launch this new Program.* The CBGP provides an extraordinary opportunity to create a funding source to support CDFIs in their mission of promoting community and economic development in underserved communities across the country. The need for long-term, patient capital to revitalize low-income neighborhoods is greater now than it ever has been. The Fund staff should be applauded for their efforts to implement this Program in the face of unprecedented economic and fiscal challenges.

We believe that CRF is in a unique position to share both its expertise and experience in accessing the capital markets as the Fund implements this Program. Many functions described in the statute are roles with which CRF has first-hand experience. For example, CRF serves as an aggregator of loans, underwriting and pooling assets originated by or through CDFIs and other community development lenders. As mentioned above, we have also assembled and issued our own Notes collateralized by community and economic development loans. These obligations may prove to be models for structuring bonds or notes issued under the CDFI Bond Guarantee Program.

Finally, CRF has substantial expertise in servicing community development assets. We act as master servicer for all of our Notes, as well as, primary servicer under contracts with more than 30 community development lenders across the country. We manage more than $613.6 million in assets on our own behalf and approximately $100 million under contract for others. CRF is the only non-profit servicer rated by Standard & Poor's, and we are an approved Fannie Mae servicer.

In reading the statutory language for the CBGP, we have found a number of key issues that should be clarified to make this Program workable. Our first concern pertains to the definition of the term "*eligible community or economic development purpose"* in section 114A (a)(2). The statute requires that a "*loan*" or "*any credit instrument extended under this Program"* must meet *"any purpose described in section 108(b)"* of the Riegle Community Development and Regulatory Improvement Act of 1994 *AND "includes the provision of community or economic development in low-income or underserved rural areas."* We believe this definition was intended to allow bond proceeds to be used to make loans that are consistent with the purposes stipulated in the Riegle Act *OR* to extend loans to eligible CDFIs. The Fund should interpret and clarify this in the regulations so as not to require a loan to meet both conditions simultaneously.

Our second concern arises around whether a qualified issuer can also be a borrower under the Program. We recommend that the CDFI Fund interpret the statute to provide for such a mechanism.

Here is the issue: In its simplest form, the CBGP is intended to get capital to CDFIs through a federally guaranteed loan so that CDFIs can use that capital to make eligible loans to end-borrowers. Such a mechanism implies the following steps:

Scenario 1- Direct Issuer

1. A CDFI acting as a qualified issuer obtains a bond guarantee from the Secretary.
2. The qualified issuer places the guaranteed bond with the Federal Financing Bank (borrows money) and obtains cash proceeds.
3. The CDFI uses the cash proceeds from the bond to make loans to end-borrowers for "eligible community and economic development purposes."

This scenario is borne out by the fact that a "*qualified issuer"* is defined as "*a CDFI or any entity designated to issue notes or bonds on behalf of such CDFI"* [1]. This language clearly indicates that a CDFI could act as its own qualified

[1] Section 114A(a)(8) of the statute defines qualified issuer as either a CDFI or "any entity designated to issue notes or bonds on behalf of such community development financial institution…" For purposes of simplicity in this illustration we are looking only at a CDFI as qualified issuer.

issuer. Such a situation is envisioned under the so called Direct Issuer model, one of three bond structures being considered by the CDFI industry.[2]

However, when one examines other various definitions in the statute, one might conclude that the qualified issuer may only use the proceeds of a federally guaranteed bond to make loans to *another* CDFI. Under the terms of the Guarantee Authorized in section 114A(b), the guarantee must be used to "ensure payment on bonds issued by the qualified issuer if the proceeds are used to make *loans* to *eligible* CDFIs."[3]

This interpretation implies the following steps:

Scenario 2 – Loan from CDFI A to CDFI B

1. "CDFI A" acts as a qualified issuer obtains a bond guarantee from the Secretary.
2. The "CDFI A" as qualified issuer places the guaranteed bond with the Federal Financing Bank and obtains cash proceeds.
3. "CDFI A" as qualified issuer uses the cash proceeds to make a loan to a different CDFI ("CDFI B").
4. "CDFI B" uses the cash proceeds from the loan to make loans to end-borrowers for "eligible community and economic development purposes."

This implies that, should a CDFI seek to obtain a guaranteed loan under the Act, it must borrow from another CDFI that is a qualified issuer. Otherwise, if a CDFI were to serve as its own qualified issuer, it would be required to make a loan to itself. The CDFI Fund should address this illogical requirement by including language in the regulations clarifying that a CDFI may serve as its own qualified issuer and allow for the use of the Direct Issuer bond structure under this Program.

One might argue that this scenario is not a problem because the CDFI can designate another entity as a qualified issuer to issue bonds or notes on its behalf. This scenario follows:

Scenario 3 – Loan from Designated Entity to CDFI

1. "CDFI A" designates "Entity A" as a qualified issuer.
2. "Entity A" obtains a bond guarantee from the Secretary.
3. "Entity A" as qualified issuer places the guaranteed bond with the Federal Financing Bank and obtains cash proceeds.

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[2] See Opportunity Finance Network's Position Paper on the CDFI Bond Guarantee Program, August 3, 2011, page 2.
[3] Small Business Jobs Act of 2010, section 114A(a)(1).

4. "Entity A" as qualified issuer uses the cash proceeds to make a loan to "CDFI A".
5. "CDFI A" uses the cash proceeds from the loan to make loans to end-borrowers for "eligible community and economic development purposes."

Given that the purpose of the CBGP is to enable CDFIs to borrow money under a federal guarantee and use the proceeds for any Riegle Act purpose including loans to end-borrowers, Scenarios 2 and 3 do not provide for such a borrowing.

Thus, third we are concerned that the implications of the situation described above are to sever the bond guarantee from the loan to the CDFI. The regulations should provide a mechanism to address this issue and allow a qualified issuer to access the federal guarantee directly. By placing an entity, either a CDFI or its designate, between the CDFI borrower and the Federal Financing Bank, the entity in the middle of the transaction now bears credit risk exposure to the ultimate CDFI borrower and must therefore have the balance sheet and capacity to bear this risk because the loan it makes to the borrower CDFI will NOT BE GUARANTEED. Few CDFIs have the balance sheet or financial capacity to make loans in $100 million increments to other CDFIs. This language implies that the qualified issuer would need to have a balance sheet of sufficient size to assume the credit risk of other CDFIs. This would dramatically limit the number organizations that could serve as a qualified issuer for this Program, and it would likely require large financial institutions to become entities designated to issue bonds or notes on behalf of CDFIs—a circumstance that could significantly change the character of the program. This is certainly not what was intended when the CBGP was passed, and CRF strongly urges the CDFI Fund not to interpret the statue in any manner other than Scenario 1 above.

Fourth, it is imperative that bond structures aggregating either end-borrower loans or loans to eligible CDFIs be feasible under this Program. The industry has proposed two such structures, the Pooled Asset-Backed Loans model and the Pooled Loans/Investments to CDFIs model. Both of these structures are essential to ensure that smaller CDFIs have access to this important new funding source, and to comply with the statutory requirement that bonds be issued in amounts of not less than $100 million. However, both models depend on the use of Special Purpose Entities ("SPEs") to aggregate *eligible loans* (to end-borrowers or to eligible CDFIs) as collateral for bonds or notes issued under this Program. We urge the CDFI Fund to deem such SPEs sponsored by otherwise eligible CDFIs and for the sole purpose of holding eligible loans as "CDFIs" for purposes of borrowing under the Program. This interpretation is essential because the Secretary may only guarantee bonds or notes if the proceeds are used to make loans to CDFIs.

Typically, an SPE takes the form of a single-member Limited Liability Company, ("LLC"). The SPE is a separate legal entity that is controlled by its sponsor. Asset-backed loans/securities are generally structured through an SPE in order to isolate their assets from other assets of the sponsor and from notes previously issued by their sponsor. CDFIs should be permitted to sell loans to the SPE on a non-recourse basis to ensure the integrity of other obligations they may have issued and to provide bondholders with clear access to collateral securing the bonds or notes.

Given the functions an SPE performs, we envision these entities serving as qualified issuers as well. To provide SPEs with maximum flexibility while still complying with the statutory language included in section 114A(b), we recommend the regulations make clear that SPEs established by CDFIs in good standing are deemed to be CDFIs for the purposes of this Program. Furthermore, these SPEs should be permitted to rely on the CDFI sponsor's history of deploying funds for eligible community and economic development uses to meet CDFI certification requirements. An analogous approach has been used under the NMTC Program where a Community Development Entity, ("CDE"), is permitted to borrow its Controlling Entity's organizational track record of lending and investing in qualified census tracts when applying for tax credit allocations.[4]

We respectfully request the CDFI Fund to include the following language in the regulations to ensure that SPEs are considered CDFIs for the purposes of this Program.

"A Special Purpose Entity, ("SPE"), or similar entity sponsored by a CDFI, in good standing, and created for the sole purpose of acquiring eligible community and economic development loans, should be deemed a CDFI under the CDFI Bond Guarantee Program. In this case, the SPE is simply an extension of the sponsoring CDFI and should be permitted to substitute the track record of the CDFI to meet the certification requirements contained in 12 CRF Part 1805.201 for the purposes of this Program."

<u>ISSUES INCLUDED IN THE REQUEST FOR COMMENT</u>
Please note we have only included issues where we offer comments.

<u>Section 1: Definitions</u>

(i) How should the term low-income be defined as such term is used in Section 114A(a)2?

We concur with the approach described by our industry colleagues. The CDFI Fund should define the term low-income as broadly as possible. While we believe that the definition of "low-income" should include low-income census tracts, the definition should be expanded to include HUD definitions that are not based on census-tracts. Often CDFIs are not able to serve low-income people who may be located in low-income areas but are not captured when the definition uses census tracts as the unit of measure.

(ii) How should the term "rural areas" be defined as such term is used in Section 114A(a)2? For example, is a rural community any census tract that is not located in a metropolitan statistical area (MSA)? Discuss how a particular definition would enable the Program to target businesses and residents in rural areas, and

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[4] CDFI Fund 2011 New Markets Tax Credit Allocation Application, Question 3, TIP, page 2.

discuss whether there are particular measures that should not be used because they may inadvertently disadvantage certain populations (i.e., provide examples of particular households or communities that would not qualify under specific definitions).

CRF strongly recommends using a new system called Rural-Urban Commuting Area Codes, ("RUCAs"), developed collaboratively by the Health Resources and Service Administration's Office of Rural Health Policy, ("ORHP"), and the Department of Agriculture's Economic Research Service, ("ERS"). The rural-urban commuting area ("RUCA") codes classify U.S. census tracts using measures of population density, urbanization, and daily commuting patterns. This system more accurately characterizes geographic areas as urban or rural.

Using a definition based on RUCAs would make it easier to target rural areas and avoid the recurring problem of inappropriately classifying many rural counties as "urban" or "non-metropolitan". St. Louis County in MN illustrates the problem many rural areas face when trying to access federal resources. Although vast portions of St. Louis County are federal wilderness areas and other areas are sparsely populated and should certainly be considered rural, under a county-based definition of rural, St. Louis is not classified as a rural area because it is in the MSA of the City of Duluth. Adopting a definition based on the RUCA codes would allow the CDFI Fund to capture *all* areas that are rural and more effectively target CBGP resources to businesses and residents of these areas.

<u>Section 2: Use of Funds</u>

(a) Criteria and Use of Funds

(i) Should there be any limitations on the types of loans that can be financed or refinanced with the bond proceeds? Are there any uses of bond or note proceeds that should be excluded or deemed ineligible regardless of the fact that the use was in a low-income or underserved rural area?

There should be no specific restrictions placed on the types of loans that can be financed or refinanced with bond proceeds other than they are used for *eligible community or economic development purposes*. Nor should the Program regulations create incentives to support particular asset classes. CDFIs should be allowed to use bond proceeds to restructure and strengthen their balance sheets by replacing short-term funds with longer-term resources. However, we believe a majority of the CBGP resources should be used to fund new eligible loans that will create jobs and contribute to growth in low-income and underserved rural communities.

Although it is tempting to prohibit the use of proceeds to finance predatory loans, it can be difficult to define what constitutes such a product. There are a number of CDFIs that offer "responsible" pay day loans or other consumer loan products, such as stored value cards, that appear predatory. However, these products serve an important function of providing higher risk borrowers with access to credit. If properly administered, these products can be safe and may help borrowers to build or repair their credit histories. One example of such a product is a payday loan coupled with financial counseling that allows a borrower to "graduate" to less expensive loan products.

We also strongly endorse the industry recommendation there be no prohibition against using the proceeds from Program in conjunction with other government programs such as the New Markets Tax Credit, the Low-income Housing Tax Credit, HOME funds or guarantee Programs offered through the Small Business Administration or the US Department of Agriculture.

(ii) Should the capitalization of: (1) revolving loan funds; (2) credit enhancement of investments made by CDFIs and/or others; or (3) loan loss reserves, debt service reserves, and/or other sinking funds in support of a federally guaranteed bond, be included as eligible purposes?

Yes, all of the purposes listed above should be included as eligible uses of bond or note proceeds to maximize the flexibility of these funds and to encompass the diverse range of CDFI financing activities.

(iii) Should there be any limits on the percentage of loans or notes refinanced with the bond proceeds? If so, what should they be?

There are two types of refinancings that should be addressed separately. The first type refers to refinancing debt on CDFIs' balance sheets. Replacing a portion of CDFIs' assets with bond proceeds would lead to stronger balance sheets, better asset liability management and additional financing capacity. We suggest that this type of refinancing be limited to not more than 50% of bond proceeds in order to encourage CDFIs to make new loans to borrowers that will retain or create new jobs in low-income communities.

The second type of refinancing involves the refinancing of existing debt of non-CDFI borrowers. Many small businesses have inappropriate debt structures that threaten their viability. CDFIs could extend new loans to replace this existing debt if such refinancing will create or preserve jobs that might otherwise be lost.

Refinancing New Market Tax Credit transactions as they reach year seven should be an eligible use of bond proceeds. Borrowers will need to find appropriate sources of take-out financing for these transactions.

(iv) Should CDFIs be allowed to use the bond proceeds to purchase loans from other CDFIs? If so, should the CDFI that sells the loans be required to invest a certain percentage of the proceeds from the sale to support additional community development activities?

Yes, the purchase of loans from CDFIs should be considered an eligible use of bond proceeds. We firmly believe the CDFI Fund should interpret the definition of a "*loan*" to include any "*credit instrument*,"[5] including *"the purchase of a*

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[5] Section114A (a)(4) of the Small Business Jobs Act of 2010.

loan or a loan originated under an advance commitment extended under the Program for any eligible community or economic development purpose." [6] Loan purchases are an important aggregation mechanism that will provide the majority of CDFIs with access to this long-term, low-cost funding. By selling loans, CDFIs will be able to increase their lending activities without being constrained by the size of their balance sheets. CDFIs may also be able to make loans to borrowers they have not previously served. Loan purchases are the most efficient way to leverage the CDFI industry to deliver credit to low-income and underserved communities.

CDFIs that sell loans should be required to reinvest the bulk of sales proceeds – perhaps as much as 95% - in eligible community and economic development loans. The remaining 5% could be reserved for administrative costs. CRF requires all of its loan sellers to sign a Qualified Seller Agreement, in which they agree to use *all* the proceeds from the sale of community or economic development loans *solely* to fund new development loans. Sellers are required to report annually on how loan sale proceeds are used.

(v) Should the CDFI Fund place additional restrictions on the awardees' loan products, such as a cap on the interest rate, fees and/or late payment penalties or on the marketing and disclosure standards for the products? If so, what are the appropriate restrictions?

No additional restrictions should be placed on awardees' loan products. CDFIs that offer consumer products must comply with existing consumer laws and regulations governing such products. For example, CDFI Banks that offer mortgages and other types of consumer loans are also subject to regulations and oversight by the new Consumer Finance Protection Bureau established under the Dodd-Frank Act. It would be redundant to add another layer of regulation. Moreover, all CDFIs must have a primary mission of promoting community development by providing equity or loans to borrowers in low-income areas and/or to targeted populations.[7] The combination of mission-driven lending/investment and existing regulations obviates the need for additional restrictions on awardees' loan products.

(b) Section 114A(c)(1) states that a capital distribution plan meets the requirements of the subsection if not less than 90 percent of the principal amount of guaranteed bonds or notes (other than the cost of issuance fee) are used to make loans for any eligible community or economic development purpose, measured annually, beginning at the end of the one-year period beginning on the issuance date of such guaranteed bonds or notes. The CDFI Fund welcomes comments regarding this provision, specifically regarding what penalties the CDFI Fund should impose if an issuer is out of compliance.

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[6] Under an advance commitment, CRF commits to buy a lender's loan or loans prior to closing based on an agreed upon set of terms, underwriting, and documentation criteria.

[7] See Section 103(20) of the Riegle Community Development and Regulatory Improvement Act of 1994 or 12 USC 4702 for the definition of Targeted Population.

If a qualified issuer falls out of compliance, there should be a cure period of 90 days before triggering the guarantee and/or the disqualification of the issuer. Where possible, the CDFI Fund should allow the issuer to cure the non-compliance by substituting an asset without history of delinquencies or other adverse action. This course of action is most likely to apply in a Pooled Asset-Backed Loans structure and perhaps in a Pooled Loans/Investments to CDFIs structure.

(c) Relending Account Funds

(i) How should the CDFI Fund define "relending" account as stated in Section 114A(c)(2)? How should it differ from the loans made under Section 114(A)(c)(1)?

If bond proceeds are used to support the financing activities of a revolving loan fund and the preponderance of the money is deployed on a consistent basis, then those resources should *not* be included in the relending account.

We concur with the industry perspective that the relending account should include unanticipated repayments and prepayments of term loans. We also agree that qualified issuers should be permitted to maintain a reasonable cushion of cash reserves in keeping with prudent liquidity and risk management practices. These cash balances should be defined as "deployed" funds, not counted as part of the relending account.

(ii) If the capitalization of revolving loan funds is deemed an allowable use of funds under Section 114A(c)(a)(4), what activities would be eligible under the relending account?

If a revolving loan fund, ("RLF"), is dormant or inactive for more than a year, with un-deployed cash greater than 50% of the original balance of the fund, then the idle funds should be included in the relending account. The purpose of the Bond Guarantee Program is to provide a source of long-term funding. In the normal course of business, the resources of an RLF should revolve and repayments used to acquire new assets. Revolving funds should *not* be classified as part of the relending account if they are being redeployed within a reasonable timeframe.

(iii) If additional reserves are held, should they be permitted to be funded from the relending account?

Yes, if an issuer chooses to hold additional reserves, they should be allowed to fund such reserves from the relending account.

(iv) Should a sinking fund, or any other reserve to allow for the payment of debt service, be permitted to be funded from the relending account?

Yes, any reserves used for debt service purposes should be permitted to be funded from the relending account.

(d) Risk Share Pool

(i) If the CDFI Fund determines there is a risk of loss to the government for which Congress has not provided an appropriation, what steps should the CDFI Fund take to compensate for this risk?

a. Should the interest rate on the bonds be increased?

No, the interest rate on the bonds should *not* be increased.

b. Should a larger risk-share pool be required?

Yes, depending on the size of the pool and the experience of the issuer, the Fund may wish to require a larger risk-share pool.

c. Should the CDFI Fund require restrictions, covenants and conditions (e.g., net asset ratio requirement, first loss requirements, first lien position; over-collateralization, replacement of troubled loans)?

No, the CDFI Fund should *not* require restrictions, covenants, or conditions such as those described above to compensate for risk of loss to the government which Congress has not provided an appropriation. Any risk of loss that arises should be accounted for through the capital distribution plan submitted by the qualified issuer and approved by the Treasury Secretary. We note that mechanisms for mitigating risk will differ based on bond structure and thus should be negotiated as part of the approval process for the capital distribution plan.

(ii) How should the CDFI Fund assess and compensate for different levels of risk among diverse proposals without unduly restricting the flexible use of funds for a range of community development purposes? For example,

a. Should the CDFI Fund take into account the participation of a risk-sharing partner? What should be the parameters of any such risk-sharing?

Yes, the CDFI Fund should take into account the participation of a risk-sharing partner. It is difficult to define the parameters of any risk-sharing, as it would depend on the nature of a given transaction.

b. Should the Fund take into account an independent, third-party credit rating from a major rating agency?

The Fund may wish to take into account an independent, third-party credit rating from a major rating agency. CRF has issued four rated asset-backed securities collateralized by affordable housing and small business loans. Having gone through the ratings process, we understand both the benefits as well as challenges of educating the major rating agencies about the unique characteristics of community development assets. Thus, while we do not believe a third-party rating should be required, there may be a need for a rating as part of an effort to confirm loss projections used to determine the appropriate level of risk share.

(iii) Are there restrictions, covenants, conditions, or other measures the CDFI Fund should not impose? Provide specific examples.

Yes.

(iv) Should the qualified issuer be allowed to set aside the three percent from the bond proceeds or should these funds be separate from the proceeds?

Qualified issuers should be allowed to set aside the three percent risk share from the bond proceeds. However, the Secretary should consider whether such funding of the risk share is appropriate in the context of the Capital Distribution Plan submitted by the issuer.

<u>Section 3: Guarantee Provisions</u>

(a) Comments related to Guarantee Provisions

(i) How should the CDFI Fund define and determine "verifiable losses of principal, interest, and call premium"?

We concur with our industry colleagues that losses of principal, interest, and call premium should be defined as failure of the issuer to make bond payments in amounts and on dates that are contractually mandated by the underlying bond documentation.

(ii) Should the CDFI Fund permit a call upon the guarantee at any point prior to the issuer liquidating the available assets? If so, under what condition should a call on the guarantee be permitted?

The CDFI Fund should permit a call upon the guarantee after the collections process has begun or is completed.

(b) Terms of the Guarantee

(i) Should the CDFI Fund set specific guidelines or prohibitions for the structure of the bond (e.g., callable, convertible, zero-coupon)?

The CDFI Fund should *not* set specific guidelines or prohibitions for the structure of the bond. Instead, the Fund should let the marketplace be creative and encourage the development of innovative models for structuring these bonds.

One mechanism that would make it much easier to use the CBGP would be to permit issuers to draw down the guarantee in amounts of less than $100 million as part of a given bond issue. This would have to be done in such a way that the guarantee would still cover no less than $100 million, but would allow issuers the ability to access the guarantee as they aggregate a reasonable volume of eligible loans.

(ii) Should bonds that are used to fund certain asset classes be required to have specific terms or conditions? Should riskier asset classes or borrowers require additional enhancements?

No. Bonds used to fund certain asset classes should *not* be required to have special terms or conditions. Qualified issuers will be required to meet the investment parameters of the Federal Financing Bank. Thus, the investor will determine the need for additional enhancements and this will be reflected in the bond structure.

(c) Limitations on the Guarantee

(i) Can qualified issuers apply for multiple issuances? Should there be a limit per qualified issuer? If so, what should that limit be?

Yes, qualified issuers *should* be allowed to apply for multiple issuances under the CBGP. No, there should *not* be a limit per qualified issuer.

Section 4: Eligible Entities

(a) Eligible Entities

(i) Should the CDFI Fund require one qualified issuer (or appointed trustee) for all bonds and notes issued under the Program?

No, the CDFI Fund should *not* appoint one qualified issuer (or trustee) for all bonds and notes issued under the Program. Issuers should be able to apply for multiple issues so as to ensure that those with expertise and capacity are not excluded after issuing one bond or note offering.

(ii) Should the CDFI Fund permit an entity not yet certified as a CDFI to apply for CDFI certification simultaneous with submission of a capital distribution plan?

No, the CDFI Fund should *not* permit entities not yet certified as a CDFI to apply for CDFI certification simultaneous with submission of a capital distribution plan. Entities seeking CDFI certification may access funding from the CBGP through the two bond structures that aggregate loans made for eligible community or economic development loans.[8] However, we wish to point out that SPEs should *not* be considered "new entities" for the purposes of the CBGP as long as their sponsors are existing CDFIs.

We also share the view of our industry colleagues that CDFIs should be certified for at least two years in order to be eligible to participate in the CBGP. CDFIs that have not been certified for at least two years should be allowed to qualify on an exception basis if they can meet appropriate mission-based criteria to ensure that proceeds are used in accordance with the intent of the statute.

(iii) Should the CDFI Fund allow all existing CDFIs to apply, or should there be minimum eligibility criteria?

Yes, the CDFI Fund should allow all existing, certified CDFIs to apply to this Program. The suitability of a CDFI to obtain the federal guarantee should be determined on a case-by-case basis by the Secretary pursuant to the quality and feasibility of the applicant's capital distribution plan.

(iv) The Act states that a qualified issuer should have "appropriate expertise, capacity, and experience, or otherwise be qualified to make loans for eligible community or economic development purposes." How should the CDFI Fund determine that a qualified issuer meets these requirements?

We concur with the industry position that at the very least, a qualified issuer must be a certified CDFI in good standing and must "demonstrate a significant and sustained track record of investing in and supporting economic development in low-income communities." We also support the notion that the Fund should carefully consider an applicant's history of lending and investing for economic and community purposes and are motivated to do so for mission-related reasons only.

The vast majority of CDFIs *do not* have the balance sheet capability to engage in the direct issue of bonds under this Program. These institutions will need to rely on CDFIs with a well established track record of aggregating community and economic development loans. Over its 23 year history, CRF has developed considerable expertise in assembling pools of affordable housing, small business and community facilities loans as well as extending loans to community development lenders. This experience is directly relevant to the two aggregation bond structures currently under discussion and should be included in the criteria used to evaluate the qualifications of qualified issuers.

We recommend that the Fund include in its regulations a CDFI's "direct experience aggregating, assembling pools of and packaging loans made for eligible community or economic development purposes," as part of the approval criteria

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[8] All three bond structures are described in Opportunity Finance Network's Position Paper on the CDFI Bond Guarantee Program, August 3, 2011, page 2.

for applicants seeking to participate in the CDFI Bond Guarantee Program. As noted above, in cases where the CDFI designates an SPE as its qualified issuer, the SPE would be permitted to use the experience of its sponsoring CDFI to meet the eligibility requirements.

(v) What penalties should be imposed if a CDFI participating in the Program ceases to be a certified CDFI? What remedies and cure periods should the CDFI Fund allow in the event of a lapse in CDFI certification?

CDFIs that lose their certification while participating in a CBGP bond issue should be given 12 months to recertify. For the asset-backed bond structures, there should be a cure period during which time the issuer can "replace" the CDFI that has lost their certification. Because of the complexity of bond issuances, these CDFIs should receive expedited consideration during the recertification process. A CDFI that is decertified should be allowed to keep its loans outstanding but should not be permitted to come back for future loans until it has been recertified.

(b) Servicing

(i) Should the CDFI Fund require one servicer for all bonds and notes issued under the Program?

No, the CDFI Fund should *not* require a single servicer for all bonds and notes issued under the Program.

(ii) Should the CDFI Fund require the master servicer and servicers to have a track record of providing similar services? How should the CDFI Fund evaluate the capabilities of prospective servicers and master servicers?

Yes, the Fund should require the master servicer and servicers to have a well established track record of providing similar services. A key factor in determining the success of the CDFI Bond Guarantee Program will be the level and skill of the servicers responsible for remitting principal and interest payments on the bonds or notes issued. Master servicers should be rated by a national rating agency and should have broad experience in servicing community development assets. This requirement will lend credibility to the bonds issued through this Program.

(iii) Should the CDFI Fund pre-qualify servicers and make those groups known to CDFIs wishing to submit a capital distribution plan for consideration?

No, it is not necessary for the CDFI Fund to pre-qualify servicers and make those groups known to CDFIs submitting a capital distribution plan for consideration. Most CDFIs do their own primary or direct servicing, or have outsourced this function to a capable organization. In addition, it would be extremely difficult to determine how to pre-qualify these servicers. As noted in 4(b)(ii), master servicers should be rated by a national rating agency. Such a rating could serve to pre-qualify master servicers and allow issuers to easily identify these firms prior to submitting a capital distribution plan.

(iv) Should a CDFI issuer be allowed to serve as its own servicer?

Yes, without question, a CDFI *should* be allowed to serve as its own servicer. Most CDFIs do service their own loans because they understand the needs and capabilities of their borrowers. CRF services its loans and has established a track record of providing "high touch" servicing to community-based organizations that prefer to outsource this function. Our clients value our unique understanding of community and economic development loans and our ability to work effectively with their borrowers.

(v) Should the master servicer be eligible to serve as a Program administrator or servicer for a qualified issuer? If so, how should potential conflicts of interest be managed?

Yes, the master servicer *should* be eligible to serve as a Program administrator or servicer for a qualified issuer. CRF functions as both a servicer and a master servicer of its loans as well as for the asset-backed securities it has issued. With regard to conflicts of interest, we suggest that the issuer retain servicing rights and have the ability to transfer those rights should a conflict arise.

(c) Qualified issuer

(i) How should a CDFI demonstrate its expertise?

If the issuer is a CDFI, the eligibility criteria discussed in section 4(iv) above should be applied. These criteria include strong mission alignment and an established track record of lending or investing in assets that meet the definition of eligible community or economic development purposes. The criteria should also take into account the extent to which a CDFI demonstrates expertise in structuring bonds and experience issuing securities backed by community development assets in the capital markets.

(ii) Are there any institutions that should be prohibited from serving as qualified issuers?

A qualified issuer should be a mission-driven organization managed or directed by the CDFI on whose behalf it is acting. The Program regulations should provide flexibility for a diverse range of issuers to participate in this Program. However, like many CDFIs, we think this Bond Program will be most effective if it is used to support participants who have a strong track record of serving low-income and underserved communities.

(iii) Should the CDFI Fund establish minimum criteria for serving as a qualified issuer?

Again, if a CDFI seeks to be the issuer, the same criteria used to determine eligibility in section 4(iv) above should be applied to the CDFI. At a minimum, CDFIs serving as qualified issuers should have a track record of making loans or investments for eligible community or economic development uses.

(iv) Should the CDFI Fund set a minimum asset size for CDFI participation as a qualified issuer?

No, the Fund should *not* set a minimum asset size for CDFI participation as a qualified issuer.

(v) Should the CDFI Fund require the issuer to have a minimum net capital (real equity capital) and require a set amount of net capital be held for the term of the bond? If so, what is a reasonable level to require?

No, the Fund should *not* set minimum net capital requirements for the issuer, *nor* should it require a set amount of net capital be held for the term of the bond.

(vi) Should qualified issuers be required to obtain an independent, third-party credit rating from a major rating agency?

No, qualified issuers should *not* be required to obtain an independent, third-party credit rating from a major rating agency. The CBGP should retain as much flexibility as possible, although the Fund should not rule out consulting with a major rating agency to persuade the Federal Financing Bank, ("FFB"), and the Office of Management and Budget, ("OMB"), that the risk share pool is sufficient to protect the federal guarantee.

<u>Section 5: Capital Distribution Plan</u>

(a) Capital Distribution Plan

(i) What elements should be required in an acceptable statement of proposed sources and uses of the funds? How should the CDFI Fund measure acceptability?

(ii) What elements should be required in a capital distribution plan? Are there examples of such plans, Federal or otherwise, upon which the CDFI Fund should model the CDFI Bond Guarantee Program's capital distribution plan requirements and application materials?

The capital distribution plan should clearly demonstrate how the issuer will deploy the bond proceeds. A pipeline of potential loans or investments and cash flow projections illustrating the ability to service the bond obligations are two key elements that should be included in a plan.

(iii) Should the CDFI Fund require specific intended uses of all the bond proceeds in the capital distribution plan or should the qualified issuers just be required to demonstrate an intended pipeline of underlying assets?

(iv) Should the CDFI Fund set minimum underwriting criteria for borrowers? Should applicants be required to demonstrate satisfaction of those criteria in the capital distribution plan?

No, the CDFI Fund should not require specific intended uses of all the bond proceeds in the capital distribution plan. Instead, qualified issuers should be required to demonstrate an intended pipeline of underlying assets to illustrate the types of loans they anticipate making. In the same way, the issuer must control the underwriting criteria for borrower loans and forecast the performance of its loans. The Fund should not set criteria but rather rely on the expertise of CDFIs to underwrite loans and investments in a fashion that is consistent with their capital distribution plan and projected cash flows of their bonds.

Section 6: Accountability of Qualified Issuers

(a) Monitoring and Evaluation

(a) What tests should the CDFI Fund use to evaluate if 90 percent of bond proceeds have been invested in qualified loans? Should reports be required from the qualified issuer more frequently than on an annual basis?

The CDFI Fund should use a test that recognizes deploying bond proceeds takes place in stages and assumes a variety of forms depending on the credit instrument. We concur with our industry colleagues that all risk-share, credit, and liquidity reserves should count as deployed assets for purposes of the 90% deployment test. All revolving loan fund facilities should also be counted as deployed assets. The test should permit closed loan facilities to count as deployed assets, not outstanding balances. Annual reporting is sufficient to appropriately monitor compliance with this requirement.

(c) What types of tests should the CDFI Fund use to evaluate satisfaction of the low-income or rural requirement set forth in Section 114A(a)(2)?

By using appropriate definitions for low-income and rural as discussed above in section 1(i) and (ii), the CDFI Fund should be able to evaluate whether these requirements are being satisfied.

(e) What specific industry standards for impact measures (businesses financed, units of affordable housing developed, etc.) should the CDFI Fund adopt for evaluating and monitoring loans financed or refinanced with proceeds of the guaranteed notes or bonds?

As chair of a committee on this issue, CRF helped to shape the response offered by our industry colleagues. We concur with the standards suggested for impact measures and support the concept of moving away from reliance on transaction-level data towards more comprehensive indicators of economic development. The Fund should collect and monitor impact data as capital reaches end-borrowers. In cases where bond proceeds are utilized to refinance debt at the CDFI level, the Fund should enforce requirements to reinvest the funds according to section 108(b) of the Riegle Act. The industry response includes a small number of data points[9] that CDFIs could self report and that could be expanded to include reporting on women and minority-owned businesses, such as husband/wife joint ownership.

In those bond structures where CDFIs are direct recipients of bond proceeds, this impact data should be required from the point at which a CDFI makes a loan/investment to an end-borrower. For structures where end-borrowers are the direct recipients of bond proceeds, this impact data should be required at the point of receipt of proceeds. This data should be collected on a prospective basis until actual data can be collected and reported on a look back basis. We also recommend that the Fund collect off-balance-sheet information to fully understand the assets managed by CDFIs through pooled bond structures involving SPEs.

(f) Should achievement of some standards or outcome measures be mandatory?

No.

(g) Are the approval criteria for qualified issuers as listed in Section 114A(a)(8)(B) adequate? If not, what else should be included?

In addition to the approval criteria for qualified issuers listed in the section 114A(a)(8), please see our comments on qualified issuer eligibility in section 4(a)(iv) above.

Section 8: Servicing of Transactions

(a) Servicing of Transactions

(i) The Act lists certain duties of a Program administrator. Should there be other requirements?

(ii) The duties of a Program administrator suggest that the CDFI Fund will serve as the Program administrator for all issuances. Should the CDFI Fund require that each qualified issuer have a designated Program administrator as suggested in section 114A(a)(7)?

We concur with the industry opinion that some of the duties listed in the Act relating to the Program administrator are not appropriate for the CDFI Fund. Specifically, bond packaging is better left to the issuer or its designate (aggregator), and certain compliance monitoring is better performed by a servicer or the issuer (or its designate/aggregator). We support the recommendation that each Bond Guarantee applicant propose the responsibilities of each party to the transaction based on the specifics of the proposed structure and use of proceeds. This would allow the CDFI Fund to act as Program administrator for a particular guaranteed bond, but delegate certain responsibilities to other parties.

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[9] See Opportunity Finance Network's Position Paper on the CDFI Bond Guarantee Program, August 3, 2011, page 19.

(iii) If so, should the servicer be eligible to serve as a Program administrator for a qualified issuer?

Yes, the servicer *should* be eligible to serve as a Program administrator and there *should be no* conflicts of interest.

(iv) Who should be responsible for resolving troubled loans?

The servicer should be responsible for servicing and resolving troubled loans. As noted above in section 3(ii), the guarantee would be called or paid out only after foreclosure or liquidation and recovery. This approach provides the servicer with an incentive to recover the full value of the loans while empowering them with the latitude and discretion necessary to achieve this outcome.

(v) On what basis should servicers be compensated?

Servicers should be compensated based on a percentage of assets serviced with a per loan floor and the ability to charge fees for certain activities, such as subordinations, calculation of pay-offs, loan set-ups, etc. This compensation will vary based on asset class and the extent of the services provided.

(vi) Are there any duties not listed that should be included in sections 114A(f)(2) through 114A(f)(4)? Are there any prohibitions or limitations that should be applied?

We concur with our industry colleagues that the "aggregation" function should be included among the duties listed in sections 114A(f)(2) through 114A(f)(4). This role is central to CRF's mission of providing capital markets resources to community-based lending organizations through the purchase and funding of community and economic development loans. As an aggregator, CRF identifies, originates/underwrites and assembles loan pools that are used to support our Revenue Notes and other securities. We model cash flows associated with these loan pools to ensure proper repayment of our obligations. In addition, aggregators like CRF, are often both servicers and master servicers for the obligations they issue and manage until maturity.

We agree these duties could be performed by a qualified issuer. Or the qualified issuer could simply be a conduit designated by a qualified CDFI and the conduit could be managed by a third-party aggregator. The aggregator does not necessarily have to be a CDFI but must work at the behest of qualified CDFIs, and would have to be qualified to perform the duties outlined herein.

<u>Section 9: General Compliance</u>

(i) What types of compliance measures should be required by the CDFI Fund? Should the CDFI Fund mandate specific reports to be collected and reviewed by the servicer and ultimately the master servicer? If so, please provide examples.

(ii) The Act states that "repayment shall be made on that portion of bonds or notes necessary to bring the bonds or notes that remain outstanding after such repayment into compliance with the 90 percent requirement of paragraph (1)." How should the CDFI Fund enforce this requirement?

(iii) What penalties should the CDFI Fund impose if a qualified issuer is deemed noncompliant?

(iv) The Act provides that the qualified issuer pay a fee of 10 basis points annually. What penalties should be imposed for failure to comply?

CRF directly contributed to shaping the industry response to this question and we concur with the recommendations offered by our colleagues at Opportunity Finance Network.

Section 10: General Comments

Any general comments and suggestions regarding the structure of the CDFI Bond Guarantee Program.

(i) The use of standardized, uniform documentation for underwriting loans aggregated under the Pooled Asset-Backed Loans and/or the Pooled Loans/Investments to CDFIs bond structures could make it easier to access the capital markets in the future should the Fund decide to allow other investors to purchase bonds or notes issued under this Program.

(ii) The presence of the Federal Financing Bank as the sole investor in CDFI guaranteed bonds has many benefits in the early years of this Program. However, neither the Act nor the Request for Public Comment mentions any proscribed role for the FFB. Not much is known about the FFB and, as such, the industry is unable to make comments about the role of this investor in the CBGP. CRF supports the position that the regulations should strongly encourage the FFB to disclose its rules, requirements, structures or constraints that could affect how the CBGP will operate, so that the industry can learn how this institution works and have input regarding its role in the Program.

CONCLUSION

Thank you for the opportunity to share our views and recommendations on this path breaking new program. The CDFI Bond Guarantee Program is the single most important new dedicated funding source for CDFIs since the Fund was established. In our view, this Program is a major step forward in helping CDFIs to reach capital markets investors – an undertaking that was derailed by the financial crisis.

We appreciate the CDFI Fund's efforts to develop and implement this Program and stand ready to assist the Staff in any way possible. Please do not hesitate to contact me with questions regarding our comments included in this letter.

Sincerely,

Frank Altman
President and CEO