



August 15, 2011

Jodie Harris
Policy Specialist
CDFI Fund
U.S. Department of the Treasury
601 13th Street, NW., Suite 200 South
Washington, DC 20005

Dear Ms. Harris:

Opportunity Finance Network appreciates the opportunity to respond to the Request for Comments on the CDFI Bond Guarantee Program, published in the *Federal Register* on July 1, 2011.

Opportunity Finance Network is the leading network of private financial intermediaries identifying and investing in opportunities to benefit low-income and low-wealth people in the U.S. Our financing delivers both sound financial returns and real changes for people and communities. Members of the Opportunity Finance Network have originated more than \$23.2 billion in financing in non-conforming urban, rural, and Native communities through 2009. This has generated or maintained 298,511 jobs; 60,261 businesses and microenterprises; 635,528 housing units; and, 6,465 community facility projects. With cumulative net charge-off rates of less than 1.4%, we have demonstrated our ability to lend prudently and productively in unconventional markets often overlooked by conventional financial institutions.

OFN was a chief advocate for the CDFI Bond Guarantee Program (CBGP) and since the passage of the legislation creating it has led the effort for prompt implementation of the program and for development of the CBPG in a way that reflects Congressional intent to support the work of CDFIs. For several years, OFN has invested significant resources toward shaping the program. Even before passage of the legislation, we consulted experts to help us understand the possibilities of the program. The hundreds of hours of staff and consultant time spent on analysis, internal education, outreach, and knowledge sharing have given OFN deep knowledge of the CBGP's potential for the industry and solid understanding of the elements critical for its success.

Following enactment of the law creating the CBGP, OFN convened the Bond Policy Group (BPG), a set of CDFI leaders who provide analysis and technical and practitioner advice on program design and structure. The members of the Bond Policy Group represent CDFIs of various sizes, strategies, geographies, and markets. The BPG has met regularly over the course of 2011 and, with the assistance of investment banking expertise, has developed a set of guiding principles that were presented to Treasury earlier this year as well as a position paper in response to the Fund's request for comments. OFN's recommendations draw heavily upon the work of this group as well as on our own history as a CDFI intermediary.

In addition to the efforts of the BPG, OFN's comments are informed by our long history as an investor in, technical assistance provider to, and collector of data about CDFIs. OFN is a 26-year leader in the



CDFI industry, with recognized best practices at underwriting, assessing risk, and lending to CDFIs and has provided cumulative financing to CDFIs of more than \$120 million, without a loss of investor capital or a write-off in our portfolio. OFN holds a diversified portfolio, by sector (housing-40%, business-35%, community facilities-16%, and consumer-9%) and geography (urban-72% and rural-28%). OFN has also conducted an annual survey of our membership for more than twenty years and manage the industry-wide CDFI Common Data Project (CDP), using that data for advocacy, consulting, CARS™ analysis, and other purposes. These activities have given OFN significant insight into CDFI underwriting, risk mitigation, and outcome measurement. They also demonstrate to us how important a resource the CBGP is and how crucial it is that its implementation best support the CDFI industry.

OFN's experience also tells us that the role of intermediaries is critical for the full benefit of the CDFI industry. An important role of OFN's Financing Fund has been to make foundation, financial institution, and public-sector capital, including from the CDFI Fund, available to CDFIs that could not directly access those capital sources themselves. A number of other institutions, such as the National Federation of Community Development Credit Unions and First Nations Oweesta Corporation, play similar roles. While many CDFIs can access capital directly, the capacity of the field to access the CBGP given the \$100 million size limitation will be constrained without the assistance of intermediaries or aggregators as described in more detail in the "General Recommendations" section of the attached responses. The infrastructure and regulations for the CBGP must support an aggregator role.

Because of the diversity of the CDFI industry and the potential new strategies the CBGP will make possible, it is imperative that the CDFI Fund apply the flexibility that is the hallmark of its other programs to the CBGP. To implement the program with this approach and to ensure the success of the CBGP, the CDFI Fund must:

- Allow for and support the participation of CDFIs of all sizes, sectors, and financing strategies. The CBGP must accommodate a variety of structures that provide for aggregation and for different kinds of roles for CDFI.
- Permit a broad range of eligible uses consistent with CDFIs' products and services. The CBGP must support uses of funds consistent with the definition of community or economic development in the CDFI Act of 1994, at 12 CFR Part 1805.301, and in the fifteen-year implementation of the Fund's Financial Assistance program. The range of uses should include but not be limited to refinancing, capitalization of a revolving loan fund, loans to and purchase of loans from other CDFIs, loan loss reserves, the required risk-share pool, debt service reserves, and/or sinking funds in support of a Federally guaranteed bond, investments of regulatory capital—all activities that are routinely undertaken by CDFIs or would be part of a strategy for prudent use of bond proceeds.
- Approve guarantees that support a capital distribution plan of \$100 million, but allow bond and note issuances of lesser amounts, over a longer period of time than 12 months, and in varying maturities and rate structures (variable and fixed).



- In considering the pooled asset-backed model structures described in more detail in the attached recommendations, allow for flexible management of cash flows associated with the asset pools to ensure prudent asset-liability and risk management.
- Consider each issue separately on its own merits with few, if any, one-size-fits-all considerations.
- Evaluate potential issuers based on their track record and capacity to deliver on proposed capital distribution plan. Base risk assessment on the loss performance and payment history of the CDFI industry, not on that of the conventional financial markets.
- Employ a toolbox of risk mitigation strategies.

In addition to these key elements that must run through all aspects of the CBGP implementation, OFN offers the attached recommendations in response to the specific questions posed by the CDFI Fund. While many of these comments are similar to those in the letter submitted by the Bond Policy Group, OFN's comments address more mechanical aspects of how the CBGP can facilitate the diversity of the CDFI industry and emphasize the importance of a program that accommodates participation by CDFIs of all sizes through aggregation.

Conclusion

The CBGP, if implemented successfully, would dramatically improve CDFI access to capital and through them, access for their communities; recapitalize CDFI balance sheets, improving profitability and financial stability; and help banks and other mainstream financial institutions increase their financing in partnership with CDFIs for the benefit of low-income, low-wealth, and other disadvantaged communities. As a result, the number of jobs created and maintained, the supply of quality, affordable housing, and access to vital community facilities and services all would increase. In short, the CBGP would give CDFIs, which are playing an increasingly central role to a wide range of financing strategies, access to a reliable supply of capital with a term and cost structure that has never before been available. Through the CBGP, CDFIs can expand their capital sources, leveraging decades of pioneering investments by private foundations, banks, the government, and others.

OFN appreciates the CDFI Fund's consideration of these recommendations. We recognize that this request for comments is one step in an ongoing process to ensure the success of the CBGP. We strongly urge the Fund to continue dialogue with the CDFI industry through both formal channels such as public comment on other bond-related documents, and less formal activities such as the conference attendance and group meetings that have been so valuable to us in the past months. Regular conversation with the industry and stakeholders will be critical to the flexible and comprehensive approach that must underlie all of the Fund's implementation decisions.

If you have questions or would like further clarification about any of our comments, please contact Jennifer Vasiloff, Executive Vice President, Policy at jvasilioff@opportunityfinance.net. We look forward



to working with the CDFI Fund to ensure the successful use of this important new resource and to the results it will bring to CDFIs and their communities.

Sincerely,

Mark Pinsky
President and CEO



OFN Recommendations on the CDFI Bond Guarantee Program

General Recommendations:

In implementing the CDFI Bond Guarantee Program (CBGP), OFN believes that the CDFI Fund should encourage a variety of bond structures, allow both fixed and variable interest rates, accommodate a broad spectrum of asset classes, and support the capital needs of a wide range of CDFIs. Each potential bond issue must be considered on its own merits. A "one size fits all" approach is not appropriate and will not work.

OFN also believes that the following bond structures seem most likely to serve the needs of the CDFI industry, although the Fund should consider additional options that demonstrate promise. The answers to some of the questions the Fund asks in the Request for Comments will differ depending on the bond structure employed. Throughout our recommendations we will be referring to these three bond structure options:

- 1) **Direct Issue:** A single CDFI would directly issue a guaranteed bond of at least \$100 million. That CDFI would then decide how to deploy the funds for eligible community and economic development uses.
- 2) **Pooled Asset-Backed Loans:** Several CDFIs would contribute at least \$100 million collectively in end borrower loan assets to a trust or special purpose entity (SPE) financed by guaranteed bond proceeds. The assets would meet the definition of eligible community and economic development uses. This would allow a wide range of CDFIs to access bond proceeds and likely reduce the need to raise substantial amounts of new equity capital.
- 3) **Pooled Loans/Investments to CDFIs:** A trust or SPE would issue a guaranteed bond of at least \$100 million backed by a pool of loans to or investments in CDFIs. This would allow a wide range of CDFIs to access the Bond on a relatively flexible basis.

Structure two and three above (Pooled Asset-Backed Loans and Pooled Loans/Investments to CDFIs) will require the use of an aggregation mechanism whereby a pool of eligible loan or investment assets that meet certain requirements and characteristics are assembled and funded with bond proceeds. Such "aggregators" might also perform certain asset pool management responsibilities during the life of the guaranteed bond. This aggregator could be the issuer or it could be a third party acting on behalf of the issuer. ***An aggregator must be a CDFI unless no CDFI has the capacity to adequately fulfill this role. If no CDFI can serve as an aggregator and/or fulfill the duties of an aggregator then the Fund might permit a non-CDFI entity to perform some duties, with the ultimate control over the use of proceeds resting with the CDFI.*** These recommendations discuss the aggregator role in more detail in response to Question 8(a)(vi).

Recommendations in Response to the Fund's July 1, 2011 Request for Public Comment

[In this section, the language from the Federal Register Notice appears verbatim followed by the ***Recommendation*** advocated by OFN.]



The CDFI Fund invites and encourages comments and suggestions germane to the mission, purpose, and implementation of the CDFI Bond Guarantee Program. The CDFI Fund is particularly interested in comments in the following areas:

1. Definitions (a) Section 114A(a) of the Act provides certain definitions applicable to the CDFI Bond Guarantee Program. In particular, Section 114A(a)(2) of the Act defines eligible community or economic development purpose as any purpose described in section 108(b) [12 U.S.C. 4707(b)] and includes the provision of community or economic development in low-income or underserved rural areas. The CDFI Fund is interested in comments regarding all definitions found in the Act as they relate to the program, including the following:

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

Recommendation: The CDFI Fund should use a definition of low-income geographies based on Metropolitan Statistical Area as defined in the CDFI Fund Authorizing Statute (7 CFR part 1805) rather than census tract. Applicants to the program should be allowed to target low-income geographies as well as low-income populations, even if the low-income populations benefitting from the financing are not located in low-income geographies, consistent with the Congressional intent for the CDFI Fund authorizing statute that both people and places in rural areas be included in eligibility criteria.

(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)? Respondents should discuss how a particular definition would enable the program to target businesses and residents in rural areas, and 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).

Recommendation: The CDFI Fund’s certification criteria and its practices include indicators that demonstrate distress in both urban and rural areas. In addition, the CDFI Fund could look to US Department of Agriculture’s definition of rural areas in 7 CFR Part 3550, which defines rural area as:

(1) Open country which is not part of or associated with an urban area.

(2) Any town, village, city, or place, including the immediate adjacent densely settled area, which is not part of or associated with an urban area and which:

(i) Has a population not in excess of 10,000 if it is rural in character, or

(ii) Has a population in excess of 10,000 but not in excess of 20,000, is not contained within a Metropolitan Statistical Area, and has a serious lack of mortgage credit for low- and moderate-income households as determined by the Secretary of Agriculture and the Secretary of HUD.

(3) An area classified as a rural area prior to October 1, 1990, (even if within a Metropolitan Statistical Area), with a population exceeding 10,000, but not in excess of 25,000, which is rural in character, and has a serious lack of mortgage credit for low- and moderate-income families.

(iii) How should the term “underserved” be defined and/or measured?



Recommendation: OFN recommends that the CDFI Fund use the Fund's authorizing statute (Sec 103) and related regulations regarding "investment areas" and "targeted populations" in defining "underserved."

(iv) Should "eligible community or economic development purpose" be defined to allow a CDFI or its designated Qualified Issuer to only invest inside the CDFI Fund Target Market that it was certified to serve?

Recommendation: No. It would be too limiting to restrict a CDFI or its designated Qualified Issuer to investments in the CDFI Fund Target Market that the CDFI was certified to serve. Investments in any distressed community are desirable and should qualify as an "eligible community or economic purpose."

2. Use of Funds

(a) The Act defines a loan as any credit instrument that is extended under the CDFI Bond Guarantee Program for any eligible community or economic development purpose. Section 114A(b) of the Act states that the Secretary of the Treasury (the Secretary) shall guarantee payments on bonds or notes issued by a qualified issuer if the proceeds of the bonds or notes are used in accordance with this section to make loans to eligible community development financial institutions (CDFIs) (1) For eligible community or economic development purposes; or (2) To refinance loans or notes issued for such purposes. The CDFI Fund invites and encourages comments and suggestions germane to the criteria and use of funds. The CDFI Fund is particularly interested in comments including the following:

(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?

Recommendation: No. There should not be any limitations on the types of loans that can be financed or refinanced with the bond proceeds. The flexibility of the CDFI Fund's CDFI Financial Assistance Program permits a wide range of activities and is an excellent model for the CBGP to emulate. (The relevant definitions appear in the CDFI Fund authorizing statute at 108 (b) and are reinforced in the regulations at 12 CFR part 1805.301.)

Any loan to a CDFI, and any loan made by a CDFI, its designate or a SPE for purposes of the CBGP, is an eligible use of funds.

There should be no prohibition against using the CBGP 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.

In practice, the bond pricing and repayment requirements will determine the most appropriate uses for the proceeds within the confines of "community and economic development" uses.

In addition, issuers should be allowed to use bond or note proceeds to fund the risk-share requirement mandated by the statute, other supplemental credit and liquidity reserves that may be needed, and upfront costs of issuing the guaranteed bond.



(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 sinking funds in support of a Federally guaranteed bond, be included as eligible purposes?

Recommendation: Yes. The capitalization of all the listed uses should be included as eligible purposes.

(1) Revolving loan funds

Many CDFIs conduct their lending business as a revolving loan fund and routinely capitalize their balance sheets with investments from the CDFI Fund. Many CDFIs conduct asset liability management in aggregate as opposed to loan by loan, and liability by liability. CDFIs don't always match fund each of their loan assets with debt liabilities, but will recycle their loan assets multiple times within the term of their liabilities. Therefore, OFN believes that bond proceeds can and should be allowed to be used in a similar manner as capital for revolving loan funds.

Examples of the kind of revolving loan fund uses that are current CDFI practice, and that would be expanded by the bond, include but are not limited to:

- **Acquisition and predevelopment real estate loans for construction of affordable housing, health clinics, and healthy food retail outlets which are usually short term in nature and taken out by construction loans and permanent mortgage loans.**
- **Small business equipment loans that amortize over a medium term and get replaced by new equipment loans.**
- **Small business working capital lines of credit whose usage revolves based on the borrower's working capital needs.**
- **Financing in markets with temporary disruptions. For example, over the last couple of years when the LIHTC market was very challenging, CDFIs were able to continue to support tax credit deals until the tax credit exchange and other programs were made available to help fill gaps.**

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

Recommendation: No. OFN believes that using bond proceeds for refinancing of all types is highly desirable. Compelling reasons include the following:

- **The CBGP's authorizing statute explicitly permits refinancing in sections 114A(a)(3) and 114A(b)(2).**
- **Refinancing can actually increase the amount of capital in the market, not simply replace existing capital, particularly if it takes the form of funding or facilitating a secondary market. If lenders know that there is a secondary market that provides them liquidity in the event that they need to convert a loan asset into cash, they are more likely to engage in more lending.**



- ***Refinancing allows lenders to more appropriately match the useful life of an asset with financing terms, such as when a long term mortgage refinances a short term real estate construction loan.***
- ***Refinancing a portion of CDFIs' balance sheets with bond proceeds could lead to more stabilized balance sheets, better mechanisms for asset liability management and more financing capacity. Existing lenders and funders to CDFIs will take assurance in knowing that CDFIs have multiple sources of capital and are not dependent on one or two funders. In fact, they are likely to be more willing to increase their financing in cases where a borrower has greater access to capital. Contrary to first impressions, using the bond to replace existing debts can actually lead to growth in CDFIs' capitalization.***
- ***For decades, CDFIs have had to structure their loan assets to meet the terms of their liabilities which at times has constrained their ability to respond to the needs of their borrowers. Given that most lenders and funders to the CDFI field lend for ten years or less, CDFIs have had to either endure asset liability mismatches, or force long term needs into short term solutions. For example, this mismatch might mean a CDFI provides 5 -7 year loans with 20 year amortizations. In order to manage the associated interest rate and duration risk, CDFIs currently have to create "buckets" limiting the dollar amount of loans they can provide for these longer term needs. Having access to 30 year bond capital will allow CDFIs to refinance their existing loan assets to more appropriately meet the needs of their borrowers.***
- ***Upon expiration of use restrictions and tax credit compliance periods on New Markets and Low Income Housing Tax Credit transactions, debt will need to be refinanced. Given that there are few sources of affordable, long term debt available to replace this type of tax credit induced debt, the CGBP would be an ideal capital source to preserve properties as affordable and sustain businesses operating in low income communities.***
- ***The capital distribution plan required by statute requires the rapid deployment of bond proceeds. This may mean that early bond issues focus more heavily on refinancing than later bond issues, as CDFIs accumulate a pipeline and build up the risk reserves required.***

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

Recommendation: Yes, CDFIs should be allowed to use bond proceeds to purchase loans from other CDFIs. Demand for financing in the communities served by CDFIs exceeds supply (as evidenced by the market demand survey and quarterly market conditions reports conducted by OFN¹) so there is no need to mandate a redeployment requirement. In March 2011, OFN and the National Federation of Credit Unions surveyed a

¹ http://www.opportunityfinance.net/store/downloads/CDFI_Market_Conditions_Q111_Report_I.pdf



broad cross-section of the CDFI industry, receiving a total of 257 responses. The survey responders identified \$55 billion in market demand, and 45% of respondents would use additional capital made available through the CBGP for deeper penetration of existing markets with existing products while 54% of respondents would use the new capital, in part, to expand into new markets and/or launch new products. Clearly, based on the need of the communities served by CDFIs, there is no need to mandate reinvestment of proceeds.

Such artificial constraints often cause unintended consequences such as forcing CDFIs to lower standards or conversely make loans that could be made by conventional lenders due to compressed timeframes for origination, closing and funding of loans and investments. For example, strict reinvestment requirements in the New Markets Tax Credit program have led to instances where redeployments met the letter of the law, but not the spirit, for fear of non-compliance.

(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?

Recommendation: No. Additional restrictions are not required. The CDFI industry has an established track record for lending responsibly, and the CDFI Fund has played an effective and efficient role in oversight in certifying CDFIs that are committed to responsible products and services. The success and growth of the CDFI field over the past thirty years is based on its reputation for offering responsible products and underwriting and lending in a responsible way.

(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.

Recommendation: OFN believes that the "not less than 90 percent" requirement should be deemed met upon receipt of bond proceeds by a CDFI, as Section 114A(a)(2)(b) defines eligible community or economic development purposes as "includ[ing] the provision of community or economic development in low-income or underserved rural areas." For example, in a direct issue structure where the issuer is a CDFI or a SPE controlled by a CDFI, the "not less than 90% percent" deployment would be met immediately. Under a pooled loans/investments to CDFI structure, the "not less than 90 percent" requirement would be met when funds are disbursed to the CDFIs participating in the pool.

In addition, the "not less than 90 percent" requirement should count binding commitments to lend rather than the actual disbursement of funds. CDFIs often make capital available to small businesses and entities engaged in new construction or real estate development in the form of revolving loans and deferred draw loans so that the borrowed funds are only supplied when needed—often over a period exceeding 12 months from the date of the binding commitment to lend. These loan products are responsive to borrower needs and



should not be excluded or disadvantaged in this program due to inflexible capital distribution definitions.

(c) Section 114A(c)(2) states that not more than 10 percent of the principal amount of guaranteed bonds or notes –, multiplied by an amount equal to the outstanding principal balance of issued notes or bonds, minus the risk-share pool amount—may be held in a relending account and may be available for new eligible community or economic development purposes.

(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(c)(1)?

Recommendation: The 10% relending account, 114A(c)(2), and the 90% deployment requirement, 114A(c)(1), work hand in hand. The purpose of the relending account is to allow CDFIs (and the SPEs in model two and three) to collect and then relend unexpected principal prepayments and expected repayments of loans and investments with maturities that are shorter than the bond maturity. It is not intended, however, to capture repayments under revolving lines of credit, since the purpose of a revolving line of credit is to allow principal outstandings to fluctuate based on the borrower’s need.

The purpose of the 90% deployment requirement is to ensure that nearly all of the bond proceeds are rapidly deployed in underserved communities. Both provisions have laudable objectives. However, issuers will need to set aside cash accounts for liquidity (to manage asset liability matching) and for credit or risk-share purposes. These cash reserves should not count as part of the relending account because it will not leave enough capacity to accommodate prepayments and shorter-term maturities. Moreover, these same cash accounts should be included in the definition of deployment for purposes of the 90% deployment requirement, because they will be needed to ensure prudent risk mitigation and cash flow management operations in the use of the bond program.

The following example illustrates our proposal:

A \$100 million bond has a \$3 million cash CDFI risk-share account, a \$500,000 cash reserve for asset liability management purposes, and a maximum of \$10 million designated as a relending account. Neither the \$3 million cash in the risk-share account nor the \$500,000 in the liquidity reserve would count toward the \$10 million relending account limit. However, both accounts would count as deployed proceeds for purposes of the 90% deployment requirement.

Ultimately, the desired outcome of enforcing these two provisions is to ensure that bond proceeds flow through to our targeted communities in a way that allows sufficient flexibility for CDFIs to prudently manage cash flow and risk. By working through CDFIs, the CBGP helps address the problem of insufficient access to capital for underserved communities. Measuring whether capital access has increased in a sustainable manner is more nuanced and complex than simply measuring principal outstanding loans or investments. OFN recommends that the Fund work with the CDFI community to create



mechanisms that accurately reflect the dynamics of responsible lending practices yet holds us accountable for increasing capital access in underserved communities.

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

Recommendation: Capitalization of revolving loan funds should definitely be deemed an allowable use of funds. An illustrative list of activities that CDFIs undertake through a revolving loan fund is provided in the answer to 2 (a)(ii). However, repayments under a revolving loan facility should be excluded from the definition of relending accounts. Since funds are lent and repaid continually over the life of the facility, repayments are normal in revolving loan funds. Borrowers are expected to draw funds only when they need them and repay them as soon as funds are available. Revolving loan fund repayments are different from repayments or prepayments under term loans and as such, should not count as balances in the CBGP's relending account. Moreover, as long as a revolving loan facility remains in force and is available for use by the borrower, irrespective of its outstanding balances, it should count as "deployed" under the 90% deployment requirement. If a revolving loan facility expires prior to the maturity of the bond, then it should be considered as part of the relending account and subject to "relending" and count as "undeployed" for purposes of the 90% deployment requirement.

As explained in the answer to 2(a)(ii), revolving loan funds can be a valuable tool for small businesses and construction projects, which lead to job creation and expansion. Definitions of relending accounts and deployment that enable the CBGP to finance such important economic development activities are consistent with statutory requirements and intent.

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

Recommendation: If additional reserves are mandated, they should be excluded from the definition of the relending account and counted as deployed for purposes of the 90% deployment requirement. Please see 2(c)(i), definition of 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?

Recommendation: If a sinking fund or other reserve is required, it should be excluded from the definition of the relending account and counted as deployed for purposes of the 90% deployment requirement. Please see 2(c)(i), definition of relending account.

(d) Section 114A(d) states that each qualified issuer shall, during the term of a guarantee provided under the CDFI Bond Guarantee Program, establish a risk-share pool, capitalized by contributions from eligible community development financial institution participants, of an amount equal to three percent of the guaranteed amount outstanding on the subject notes and bonds.

(i) In the event that the CDFI Fund determines that 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?
- b. Should a larger risk-share pool be required?



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)?

Recommendation: If the CDFI Fund determines that the risk of loss is greater than 3% and Congress has not appropriated additional funds for losses, the Fund should first consider whether fees collected as specified in 114A(g) or monies appropriated in Section 1703 are sufficient to mitigate expected losses. OFN strongly believes that Congress has already appropriated \$13.5 million to the CDFI Fund in part for the purpose of risk mitigation. Risk mitigation is a standard feature of program administration, and especially critical in the nascent stages of program implementation. If those fees and appropriated funds are insufficient, then the Fund should work with the qualified issuer or applicants to utilize a "toolbox" of credit enhancements to compensate for additional risk. Some examples of risk mitigation tools are:

- Over-collateralization
- Affirmative covenants
- Third party guarantees and/or bond insurance
- Potential recourse to the originating CDFIs
- Increased interest rates on loans or investments made by the qualified issuer to CDFIs or end-borrowers. This excess spread would then be used to fund reserves that could be used to mitigate losses.
- ***A supplemental risk-sharing mechanism: the Fund could create other cash reserve pools in addition to 3 percent risk-share pool. This additional cash reserve could be funded from sources including bond proceeds, third-party CDFI investors, or investment cash flows.***

The length of time that the risk-share pool should remain intact depends on the issuing structure of the bond. Because bond risk can be more easily determined after some years of seasoning, the Fund should allow a lower risk-share for more seasoned issues where justified by bond performance.

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



Recommendation: The CDFI Fund should evaluate each application based on its individual merits. The Fund should make use of expert resources within and outside of the Federal government with experience in underwriting community and economic development transactions. The Fund should also consider the historical loss data of the CDFI industry. Where available, it should look at performance history of CDFIs at the asset level. These data are significantly more valuable than any proxy developed from data available regarding conventional markets. The CDFI marketplace is different and we do business very differently.

As part of the application process, applicants should be expected to quantify the risk in their proposal and demonstrate their ability to cover this risk.

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

Recommendation: As each issue will be considered separately and its specific goals and structure will vary from others, it is difficult to envision the specific covenants or conditions that might or might not be suited to each one. The CDFI Fund should work with the qualified issuer or applicants to utilize a "toolbox" of credit enhancements to mitigate risk including affirmative covenants or other measures.

(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?

Recommendation: The Fund should allow for the risk-share pool to be funded from various mechanisms including but not limited to: bond proceeds, third-party CDFI investors, or investment cash flows (e.g. the spread between assets earned and cash required to service the bond).

3. Guarantee Provisions

(a) Section 114A(a)(3) defines a guarantee as a written agreement between the Secretary and a qualified issuer (or trustee) pursuant to which the Secretary ensures repayment of the verifiable losses of principal, interest, and call premium, if any, on notes or bonds issued by a qualified issuer to finance or refinance loans to eligible CDFI. The CDFI Fund invites and encourages comments and suggestions relating to the guarantee provisions, especially:

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

Recommendation: Losses of principal, interest and call premium should be defined as failure of the issuer to make bond payments in the amounts and on the dates that are contractually mandated by the underlying bond documentation. The guarantee should cover both variable and fixed interest rates. The guarantee should also cover any "make-whole" premium owed the investor in the event of a prepayment (including one caused by default) of bond or note principal.



(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?

Recommendation: Yes. In order to preserve the investor benefits of bonds bearing a US Government Guarantee, bond payments must be made as contractually due in regard to both amounts due and due dates. The investor must be insulated from any problem the pool of assets or issuer is experiencing.

When evidence exists that the issuer is unlikely to pay when contractually obligated, then the guarantee should be exercised and the CDFI Fund should ensure payments are made as contractually required, much like how bond insurance operates. The CDFI Fund should work with the issuer, aggregator, and originator/servicer to exercise all rights, remedies, and restructuring opportunities before the bond structure is accelerated, assets liquidated or the bond balance reduced.

Examples of such remedies would include the substitution of non-performing assets, liquidation of underlying collateral, liquidation of risk-share and supplement credit reserves, and exercise of recourse if available.

The government should work with the issuer/aggregator to ensure minimal losses and stabilization of the rest of the asset pool or issuer's remaining obligations. If necessary, the government should also consider using the services of a special servicer to deal with nonperforming assets.

(b) Section 114A(e)(1) indicates that the Treasury guarantee shall be for the full amount of a bond or note, including the amount of principal, interest, and call premiums not to exceed 30 years. The Treasury may not guarantee any amount less than \$100 million per issuance.

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

Recommendation: The CDFI Fund should not set specific prohibitions for the structure of the bond. The following bond structures seem most likely to serve the needs of the CDFI industry, although the Fund should consider additional options that demonstrate promise.

- 1) Direct Issue: A single CDFI would directly issue a bond of at least \$100 million. That CDFI would then decide how to deploy the funds for eligible community and economic development uses.**
- 2) Pooled Asset-Backed Loans: Several CDFIs would contribute at least \$100 million collectively in end borrower loan assets to a trust or special purpose entity (SPE) that is financed by guaranteed bond proceeds. The assets would meet the definition of eligible community and economic development uses. This would allow a wide range of CDFIs to access bond proceeds and likely reduce the need to raise substantial amounts of new equity capital.**
- 3) Pooled Loans to CDFIs: A trust or SPE would issue a bond of at least \$100 million backed by a pool of loans to or investments in CDFIs. This would allow a wide range of CDFIs to access the Bond on a relatively flexible basis.**



The latter two structures are critical to ensuring that CDFIs of all sizes can participate in the CBGP.

The immediate needs of underserved markets as well as the long-term sustainability of CDFIs and the CDFI Bond Program require that CDFIs are able to create structures appropriate to their financing strategies based on market conditions and needs. To further ensure the best use of flexible capital by CDFIs, the structure of the bond options should include variable rate, fixed rate and multi-modal bonds that may initially bear a variable rate but may later convert to a fixed rate for a period of time and back to varying rate irrespective of which bond structures is used. Additionally, the CBGP should allow separate fixed and variable rate tranches in one guarantee structure to accommodate the liquidity requirements associated with risk reserves and revolving loans, and longer-term capital associated with funding longer-term loans.

OFN also encourages the Fund, consistent with the Act, to approve allocations of guarantees in the amount of \$100 million while allowing guaranteed bonds to be drawn down in amounts less than \$100 million. Bonds could be issued in smaller increments as part of one guarantee application as long as each guarantee covered no less than \$100 million of bonds in aggregate. Very few CDFIs have balance sheets large enough to qualify for the direct issue of \$100 million. Most CDFIs will likely participate in the CBGP through either the pooled asset-backed loan or pooled loans/investments to CDFIs structure. While pooled proposals can amply demonstrate the need for a combined \$100 million in guarantee authority, the coordination and timing of the issuance of \$100 million by multiple parties may not be possible in a single issuance of bonds or notes. Even when there is one direct issuer for the entire \$100 million, the nature of the loans made by CDFIs may make issuance and drawdown of the notes or bonds over time, rather than all at one time, more desirable to better match the loans made to end users and to minimize negative arbitrage and preserve the liquidity and financial strength of the CDFIs borrowing under the CBGP. Therefore, while it is reasonable for the guarantee authority to be approved in \$100 million increments, this should not prohibit the bonds and notes backed by the guarantee from being issued in smaller increments and over time.

(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?

Recommendation: No specific terms or conditions should be required at the programmatic level. Every application should be analyzed individually on an application-by-application basis. There should be no minimum terms or conditions. As it has over the past 15 years to great effect, the Fund should entrust CDFIs to make end-borrower risk assessments. Under a direct issue or pooled loans to CDFIs bond structure, the financial wherewithal of the CDFI should be analyzed to determine whether a CDFI qualifies to participate in a CBGP bond issue and whether supplemental credit enhancements might be necessary. In these



cases, the Fund should apply the loss and payment experience of the CDFI as indicators of risk as opposed to conventional market indicators.

As part of its review of capital distribution plans, the Fund should account for different asset classes when considering the terms and conditions of a bond issue. For example, in a pooled-asset backed structure the Fund will likely want to consider the extent to which the asset pool aligns with the maturity of the bonds being issued. The Fund may also want to consider whether there is adequate liquidity available to deal with the maturity of the underlying assets and repay the bonds.

(c) Section 114A(e)(2) states limitations on the guarantees. (1) The Secretary shall issue not more than 10 guarantees in any calendar year under the program. (2) The Secretary may not guarantee any amount under the program equal to less than \$100 million but the total of all such guarantees in any fiscal year may not exceed \$1 billion.

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

Recommendation: The Fund should implement the CBGP in a manner that accommodates and reflects a broad cross-section of the CDFI industry and not allow concentration among a non-diverse group of participants. The best way to do this may be to limit CDFIs to one application per round.

4. Eligible Entities

(a) Section 114A(a)(1) defines an eligible entity as a CDFI (as described in section 1805.201 of title 12, Code of Federal Regulations, or any successor thereto) certified by the Secretary that has applied to a qualified issuer for, or that has been granted by a qualified issuer, a loan under the program. The CDFI Fund welcomes comments on issues relating to eligible entities, particularly with respect to the following questions:

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

Recommendation: The Fund should not require one qualified issuer (or appointed trustee) for all bonds and notes issued under the program because doing so would prevent multiple CDFIs from becoming direct issuers.

(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?

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

(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?

Recommendation: The CBGP represents our nation's strong commitment to community development finance and CDFIs, and possibly its largest investment. As such, qualified bond issuers should demonstrate a significant and sustained track record of investing in



and supporting economic development in low-income communities. CDFIs must meet the statutory and regulatory requirements for CDFI certification and that selection criteria should select those most qualified from those less qualified for the purposes of the CBGP.

The Fund should structure the CBGP application process in a manner that advantages applicants whose organizational activity aligns closely and consistently with eligible community and economic uses contained in 12 CFR part 1805.301. In cases where a bond issue is structured through a SPE, the Fund should apply these principles to the CDFIs participating in the bond issue under the SPE. CDFIs created expressly for the purpose of qualifying for the CBGP should not be eligible to participate in the program. As such, the Fund should use care in determining that applicants have a history of lending and investing for economic and community purposes and are motivated to do so for mission-related reasons only.

In considering newly certified CDFIs, to ensure that they are not entities certified solely for purposes of qualifying for the CBGP, the Fund should consider:

- CDFIs that use mission and track record in low-income communities as the primary means to make decisions about the eligibility of these institutions;***
- CDFI with strategies and operations align strongly with their community and economic development mission;***
- The effective deployment of CDFI operational and financing resources in pursuit of their mission;***
- Clear CDFI accountability to a low-income market and a demonstrated history of working successfully in that market;***
- CDFIs that accurately track appropriate output data and continuously track outcome measurements.***

For CDFIs that are part of or controlled by another corporation(s), the other corporation(s) must also have a primary mission of community development, consistent with the Act creating the CDFI Fund.

For the purposes of the CBGP, SPEs should not be considered "new entities," since they are designates of existing CDFIs and for purposes of the CBGP, controlled by CDFIs.

Separately, the structure of the bond issue in question should also be considered:

- Direct Issue: under this structure, eligibility requirements should be applied to the issuing CDFI. The Fund has a long history of assessing CDFI performance capacity through its FA and TA programs, and as such, the existing standards provide an appropriate measure of experience, expertise, and capacity in delivering economic development services to low-income communities. It is important that the definition of an "experienced, expert, and capable" CDFI is uniform across Fund programs.***



- ***Pooled-Asset-Backed Loans: under this structure, CBGP eligibility requirements should apply to the CDFIs that are originating (and likely servicing) asset-backed loans to the SPE. Here OFN points to Sec. 107(a) of the CDFI Fund authorizing statute as the principal source of determining whether a CDFI has the experience, expertise, and capacity necessary to participate in the CBGP. CDFIs originating loans that are part of this structure should demonstrate the organizational capacity to execute their respective role in an asset-backed bond, e.g. the ability to originate loans in the time period proposed, underwrite to the standards that the issuer or aggregator requires, have the appropriate systems in place to manage their loans after origination, etc.***

- ***Pooled Loans to/Pooled Investments in CDFIs: in this model, there are likely two levels of eligibility criteria. First, the aggregating CDFI would have to meet the qualifications required to manage and make loans to other CDFIs. Separately, CBGP programmatic qualifications should also apply to the CDFIs receiving loans from the aggregator.***

In general, in addition to the criteria outlined above, both "pool" structures require the issuer/aggregator CDFI (or its designate) to show that they are experienced (or can acquire staff with experience or partner with experienced entities) in packaging loans and managing portfolios successfully.

(v) What penalties should be imposed in the event that 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?

Recommendation: CDFIs that lose their certification while participating in a CBGP bond issue should be given 12 months to recertify. For asset-backed bond structures, there should follow a cure period wherein the issuer can "replace" the CDFI that lost their certification. Because of the complexity of bond issuances, these CDFIs should receive expedited consideration during the recertification process.

(b) Section 114A(a)(5) defines a master servicer as an entity approved by the Secretary in accordance with subparagraph (B) to oversee the activities of servicers, as provided in subsection (f)(4).

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

Recommendation: No, the Fund should not require only one Master Servicer, but in the interest of keeping program costs as low as possible, the Fund may choose to limit the number of servicers used. Moreover, the Fund may decide a single Master Servicer is the most cost effective manner to administer the CBGP, but only if it can ensure maintenance of the necessary flexibility to accommodate the diversity of the CDFI industry.

(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?



Recommendation: Yes, servicers should be able to show a successful track record of managing the cash flow and performance of a portfolio of loan assets, as defined in 114(a)(5) and 114(f)(3).

The Fund should also develop and include a role for the "special servicing" of collections in the case of nonperforming loans that need restructuring and work out. Special Servicers could be appointed by the existing servicers or the program administrator, or one of the existing servicers could perform the duties of work out if qualified and agreed upon by the Fund.

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

Recommendation: OFN believes that CDFIs that originate loans financed with guaranteed bond proceeds are best positioned to service their own loans. Therefore, the notion of prequalifying all servicers is not necessary.

However, OFN believes that the Fund could pre-qualify Master Servicers and make them known to CDFIs prior to submission of an application. As part of the underwriting process for a guaranteed bond issuance, all servicers should be certified as qualified to perform duties outlined in the capital distribution plan or application. However, the number of pre-qualified Master Servicers should not be fixed for the life of the program but potentially be a dynamic and growing universe of entities capable of assisting CDFIs implement the CBGP successfully.

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

Recommendation: CDFIs issuers should be allowed to serve as their own servicers. Again, OFN believes that one of the CDFI industry's strengths—and a key to success—is in loan servicing capabilities. Patient, hands on attention paid to borrowers who may be struggling but who are still capable of meeting their debt obligations has contributed to the strong payment history of CDFIs over the past three decades.

(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?

Recommendation: There are certain responsibilities assigned to the program administrator which could be delegated to a third party, potentially the Master Servicer, the issuer, or the aggregator. The CDFI Fund or program administrator should maintain the right to replace the entity to which these responsibilities have been delegated to manage potential conflicts of interest.

(c) Section 114(a)(8) defines qualified issuers as a CDFI (or any entity designated to issue notes or bonds on behalf of such CDFI) that meets certain qualifications: (1) Have appropriate expertise, (2) have an acceptable capital distribution plan, and (3) be able to certify that the bond proceeds will be used for community development.

(i) How should a CDFI demonstrate its expertise?

Recommendation: If the issuer is a CDFI, the same criteria used to determine Eligible CDFIs in Section 4(iv) should govern qualified bond issuers. At minimum, a qualified issuer



should be a certified CDFI in good standing (or a qualified entity designated and controlled for purposes of this program by a certified CDFI in good standing) and can be for-profit or non-profit. The Fund should structure the CBGP application process in a manner that advantages applicants whose organizational activity aligns closely and consistently with eligible community and economic uses contained in 12 CFR part 1805.301. In cases where a bond issue is structured through a SPE, the Fund should apply these principles to the CDFIs participating in the bond issue under the SPE; the SPE should be considered a subsidiary or controlled entity, leaving the ultimate control of the use of proceeds with a CDFI to ensure compliance with the law's intent that the CBGP operate through CDFIs. CDFIs created expressly for the purpose of qualifying for the CBGP should not be eligible to participate in the program. As such, the Fund should use care in determining that applicants have a history of lending and investing for economic and community purposes and are motivated to do so for mission-related reasons only.

In considering newly certified CDFIs, to ensure that they are not entities certified solely for purposes of qualifying for the CBGP, the Fund should consider:

- CDFIs that use mission and track record in low-income communities as the primary means to make decisions about the eligibility of these institutions;***
- CDFI with strategies and operations align strongly with their community and economic development mission;***
- The effective deployment of CDFI operational and financing resources in pursuit of their mission;***
- Clear CDFI accountability to a low-income market and a demonstrated history of working successfully in that market;***
- CDFIs that accurately track appropriate output data and continuously track outcome measurements.***

For CDFIs that are part of, or controlled by, another corporation(s), the other corporation(s) must also have a primary mission of community development.

For the purposes of the CBGP, SPEs should not be considered "new entities," since they are designates of existing CDFIs. The SPEs should be considered subsidiary or controlled entities, with the "principal" CDFI responsible for the use of proceeds.

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

Recommendation: The Fund should exercise good judgment in ensuring that qualified issuers represent the range of diversity in the CDFI industry and that no single issuer should dominate the CBGP. Assuming applicants meet the eligibility criteria consistent with the CDFI Fund Authorizing Statute the Fund should not promulgate rules that prohibit any institution from serving as a qualified issuer.

The CDFI Fund's programs have been less successful when important mission and accountability criteria have been given lower priority in its decision-making. For example, New Markets Tax Credit subsidies have been most successful when deployed through



institutions with a strong track record in underserved communities, and strong mission screens for targeting deals. Generally, organizations that have been certified CDFIs for a short period of time should not be eligible unless they can demonstrate strong mission criteria outlined in 4(iv) that indicate a commitment to and track record in the intended uses for the bond proceeds.

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

Recommendation: If the issuer is a CDFI, the same criteria used to determine Eligible CDFIs in Section 4(iv) should govern qualified bond issuers. If a CDFI designate is the issuer, then the CDFI that is sponsoring the bond and designated the issuer should meet this criteria. At minimum, a qualified issuer should be a certified CDFI in good standing and can be for-profit or non-profit. The Fund should structure the CBGP Application in a manner that advantages applicants whose organizational activity aligns closely and consistently with eligible community and economic uses contained in 12 CFR part 1805.301. In cases where a bond issue is structured through a SPE, the Fund should apply these principles to the CDFIs participating in the bond issue under the SPE. The Fund should consider the SPE a subsidiary or controlled entity of the CDFI, and the CDFI the principal with whom ultimate control of the use of proceeds lies.

CDFIs created expressly for the purpose of qualifying for the CBGP should not be eligible to participate in the program. As such, the Fund should use care in determining that applicants have a history of lending and investing for economic and community purposes and are motivated to do so for mission-related reasons only.

In considering newly certified CDFIs, to ensure that they are not entities certified solely for purposes of qualifying for the CBGP, the Fund should consider:

- CDFIs that use mission and track record in low-income communities as the primary means to make decisions about the eligibility of these institutions;***
- CDFI with strategies and operations align strongly with their community and economic development mission;***
- The effective deployment of CDFI operational and financing resources in pursuit of their mission;***
- Clear CDFI accountability to a low-income market and a demonstrated history of working successfully in that market;***
- CDFIs that accurately track appropriate output data and continuously track outcome measurements.***

For CDFIs that are part of, or controlled by, another corporation(s), the other corporation(s) must also have a primary mission of community development.

For the purposes of the CBGP, SPEs should not be considered "new entities," since they are designates of existing CDFIs. In such cases, the SPEs are acting on behalf of CDFIs and the ultimate control of the use of proceeds must remain with the CDFI.



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

Recommendation: The Fund should not apply minimum asset standards to CDFI participation as a qualified issuer nor as a participant in any bond structure.

(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?

Recommendation: The Fund should not require minimum net capital standards for CDFI participation as a qualified issuer nor as a participant in any bond structure at the programmatic level. Required net asset levels should be determined based on the risk profile and structure of each bond application.

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

Recommendation: Qualified issuers should not be required to obtain a credit rating from a major third-party rating agency. The major third-party ratings industry is not knowledgeable about the CDFI industry and OFN is highly skeptical of their ability to accurately rate bonds issued by CDFIs. The history of third-party ratings agencies shows that newly rated industries aren't rated appropriately. At best, third-party raters would apply non-comparable criteria to CDFI investment portfolios, likely resulting in bonds ratings that do not reflect the true risk of the bond investment.

As part of its efforts to support the work of CDFIs, the Fund should take a gradual approach to moving the community development finance industry towards the ultimate goal being rated by major third-party rating agencies. In doing so, the Fund may want to consider utilizing existing CDFI ratings tools, such as the CDFI Assessment and Ratings System (CARS™), or a partnership between CARS™ and a major third-party rating agency. This partnership could eventually lead to bond issues being rated by major third-party raters on a "look-back basis." Bonds rated on a "look-back basis" could then be sold to private investors.

5. Capital Distribution Plan

(a) Section 114A(a)(8)(B)(ii)(II) states that a qualified issuer shall provide to the Secretary: (aa) an acceptable statement of the proposed sources and uses of the funds and (bb) a capital distribution plan that meets the requirements of subsection (c)(1). The CDFI Fund seeks comments relating to the capital distribution plan requirement, specifically:

(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?

(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?



Recommendation: The requirements of a capital distribution plan should depend on the bond structure proposed. In general, applicants should be able to demonstrate an intended pipeline of underlying assets and cash flow projections that illustrate the ability to service the guaranteed bond based on the expected terms and conditions of the assets in the pipeline.

(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?

Recommendation: No, the CDFI Fund should not set minimum underwriting criteria for end-borrowers. CDFIs specialize in understanding risk in markets that are outside of the financial and economic mainstream, with a remarkable record of success and minimal losses and delinquencies. The Fund should rely on this unique experience by continuing to allow CDFIs to make the best decisions regarding the needs of their community.

6. Accountability of Qualified Issuers

(a) The CDFI Fund welcomes comments on how to monitor the use of proceeds and financial performance of qualified issuers, particularly with respect to the following questions:

(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?

Recommendation: All risk-share, credit and liquidity reserves should count as deployed assets for purposes of the 90% deployment test. In addition, all revolving loan fund facilities (such as working capital lines of credit for small businesses or real estate developers) should be counted as deployed assets for purposes of this test. Lastly, binding commitments to lend should count as deployed assets, not outstanding balances. As explained in Section 2(c) in conjunction with the mechanics of the relending account, OFN doesn't believe that the 90% deployment provision should be interpreted to deny small businesses and construction projects the short term capital they need to create new jobs or lead to imprudent guaranteed bond structures due to the failure to include risk mitigation reserves.

To enable maximum responsiveness to borrower needs and provide maximum flexibility in managing liquidity and asset liability matching, OFN believes that the 90% deployment test should not be applied more frequently than once per year.

(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)?

Recommendation: The CDFI Fund's certification criteria and its practices include indicators that demonstrate distress in both urban and rural areas. If evaluating other rural activities, the CDFI Fund should use a definition of low-income geographies based on Metropolitan Statistical Area rather than census tract. Applicants to the program should be allowed to target low-income populations as well as low-income geographies.

The CDFI Fund should use the US Department of Agriculture's definition of rural areas as defined in 7 CFR Part 3550, which defines rural area as:

(1) Open country which is not part of or associated with an urban area.



(2) Any town, village, city, or place, including the immediate adjacent densely settled area, which is not part of or associated with an urban area and which:

(i) Has a population not in excess of 10,000 if it is rural in character, or

(ii) Has a population in excess of 10,000 but not in excess of 20,000, is not contained within a Metropolitan Statistical Area, and has a serious lack of mortgage credit for low- and moderate-income households as determined by the Secretary of Agriculture and the Secretary of HUD.

(3) An area classified as a rural area prior to October 1, 1990, (even if within a Metropolitan Statistical Area), with a population exceeding 10,000, but not in excess of 25,000, which is rural in character, and has a serious lack of mortgage credit for low- and moderate-income families.

(d) What support, if any, would applicants and awardees like to receive from the CDFI Fund after having issued a bond?

(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?

Recommendation: Investment in a CDFI begins a chain of activity that ultimately finances small businesses, affordable housing, commercial development, and community economic growth.

In addition to collecting data on the dollar amount of investments financed and/or refinanced, OFN recommends using standard industry indicators used by the CDFI Fund and all major CDFI trade associations today, including:

- Number of Businesses Financed, broken down by minority, female and low-income, if permitted by law to be reported

- Number of Microbusinesses Financed, broken down by minority, female and low-income, if permitted by law to be reported

- Number of Jobs created

- Number of Jobs maintained



- Number of Jobs assisted

- Number of Community services facilities financed

- Number of Healthcare slots created

- Number of Healthcare slots retained

- Number of Childcare slots created

- Number of Childcare slots retained

- Number of Educational slots created

- Number of Educational slots retained

- Number of Housing units created

- Number of Housing units renovated

- Number of Housing units assisted

- Percent of Affordable Cumulative Housing Units

- Number of Mortgages Closed



- Number of First-time buyer mortgages closed

- Number and dollar amount deployed to meet basic credit needs of low to moderate income households

- Estimated interest savings achieved by low to moderate income consumers as a result of CDFIs charging more affordable interest rates

The Fund should also track markets served:

- Percent major urban

- Percent minor urban

- Percent rural

- Percent female

- Percent minority

- Percent low-income

The Fund should also consider expanding the definition of "women-owned" businesses to include husband/wife joint ownership.



These data are available from most if not all CDFIs and provide the information necessary to paint a general picture of the scope, activities, diversity, and outcomes of the CBGP. This information should be collected for all loans financed or refinanced under the CBGP, including off-balance sheet activity, and should be collected at the institution level rather than at the transaction level.

In those 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 bond structures where end borrowers are the direct recipients of bond proceeds, this impact data should be required at the point of receipt of bond proceeds.

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

Recommendation: Achievement of the same one-size-fits-all standards or outcome measures should not be mandatory. Measurement of impact is a complex undertaking, and the extent of impact varies considerably from community to community and from transaction type to transaction type. It is inadvisable to apply an impact standard a priori across a program as diverse as the CBGP. The standards and outcomes will depend on the financing activity and assets and/or bond model.

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

Recommendation: In addition to the approval criteria mentioned in this Section, the Fund should incorporate the entity eligibility criteria cited in the answer to 4(a)(iv) of this document.

7. Prohibited Uses

(a) Section 114A(b)(5) provides certain prohibitions on use of funds including, "political activities, lobbying, outreach, counseling services, or travel expenses." The CDFI Fund encourages comments and suggestions germane to prohibited uses established in the Act, specifically as to whether there are other prohibited uses that the CDFI Fund should include.

Recommendation: No additional prohibitions are suggested.

8. Servicing of Transactions

(a) Section 114A(f) states that, in general, to maximize efficiencies and minimize cost and interest rates, loans made under this section may be serviced by qualified program administrators, bond servicers, and a master servicer. This section further outlines the duties of the program administrator, servicers, and the master servicer. Comments regarding the servicing of transactions are welcome, specifically:

- (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)?

Recommendation: While some of the duties listed in the Act relating to program administrator may be appropriate for the CDFI Fund, others are not necessarily appropriate. For example, 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). Therefore, OFN recommends that each CBGP applicant propose the responsibilities of each party based on the specifics of the proposed structure and use of proceeds. That way, the CDFI Fund could act as program administrator for a particular guaranteed bond, but delegate certain responsibilities to other parties.

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

Recommendation: In cases where the CDFI Fund delegates certain program administrative duties to a third party, said third party should be able to serve as a servicer.

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

Recommendation: In the case of troubled loans in the pool backing the guaranteed bond, a special servicer could be appointed. However, the guarantor should make this determination only after concluding that the originator (if serving the role of servicer)/issuer/aggregator is no longer competent or able to resolve the troubled situation.

(v) On what basis should servicers be compensated?

Recommendation: The compensation should be market based and determined on an application by application basis. Generally speaking, the basis should be either (a) a percentage of assets or (b) the number of loans in the pool that is backing the guaranteed bond. It is difficult to set this requirement a priori because the servicing complexity of different kinds of bond structures will vary.

(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?

Recommendation: The duties of "aggregation" are not addressed specifically in the statute but should be included in these sections. Duties of an aggregator include: (a) creating the framework for an asset pool, (b) identifying and originating the loans that will go into the asset pool, (c) developing projections that will support repayment of the bond and (d) managing the asset pool through the maturity of the bond. 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. These duties should be performed by a CDFI unless no CDFI has the capacity to adequately fulfill this role. If no CDFI can serve as an aggregator, then the Fund might permit a non-CDFI, subsidiary or controlled entity to perform some duties, with the ultimate control over the use of proceeds resting with the CDFI.

9. General Compliance



The CDFI Fund welcomes comments on general compliance issues related to monitoring the guarantee portfolio, particularly with respect to the following questions:

- (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?

Recommendation: Compliance measures under the CBGP should consist of “bright line” tests that are distinct from impact/outcome measurements. Along with the prohibitions on use of funds in 114A(b)(5) and the 90 percent deployment requirement in 114(A)(c)(1):

- ***All CDFIs participating in a bond issue at the direct issuer or SPE/ collaborative level should submit financial reports annually to the Fund at the end of the CDFI’s fiscal year.***
- ***In cases where a SPE will be the bond issuer, compliance measures should be applied to participating CDFIs as a whole—not on an individual basis.***
- ***In the event of non-compliance of a qualified issuer, there should be a cure period of at least 90 days.***
- ***If the Fund must enforce repayment of the bond due to expiry of all cure periods associated with failure to meet the 90 percent deployment requirement, it should do so in a way that preserves the remaining outstanding of the bond at its original terms (e.g., same coupon, same remaining term, etc.) and releases a proportional amount of risk-share or other credit reserves to maintain the original risk profile of the guaranteed bond.***
- ***The Secretary of Treasury should reserve the right to permit extensions of the cure period based on facts and circumstances, upon reasonable request.***
- ***The 10bps administration fee should be priced into the bond issuance.***

10. General Comments

The CDFI Fund is also interested in receiving any general comments and suggestions regarding the structure of the CDFI Bond Guarantee Program that are not addressed above.

Recommendation:

1. The presence of the Federal Financing Bank as the sole investor of CDFI guaranteed bonds has many benefits in the beginning years of the CBGP. However, neither the Act nor the Request for Public Comments mentions any prescribed 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 the FFB in the CBGP. OFN strongly requests that if the FFB has rules, requirements, structures or constraints that could affect how the CBGP will work, that the industry be



allowed to give input regarding the FFB's role and the opportunity to make public comment. OFN also recommends that requirements of the FFB, if any, for purchase of bonds or notes—such as restrictions on prepayment— be compatible with the requirements of the CBGP or that the CDFI Fund accommodate these requirements in the rules.

2. OFN encourages the Fund to maintain an ongoing dialogue with stakeholders regarding implementation issues, particularly given the short timeline made available to comment on a large volume of complicated questions. As OFN learns more about the program and more thoroughly understands the Fund's implementation of the program, we may refine our recommendations based on new information or possibilities.

To the extent possible, and without delaying the timely implementation of the CBGP, the Fund should provide opportunities to comment on the:

- Interim final rule to be issued by the end of September 2011;
- Bond Issue application materials;
- Application materials for the master servicer;
- Format and requirements of the capital distribution plan;
- Reporting and compliance instruments and mechanisms.
- Any other application and/or required materials related to the Bond Guarantee Program.

3. While the statute provides for one year after issuance for implementation of the program, the CDFI Fund should implement the program by December 31, 2011. Strong demand from CDFIs exists for the capital the CBPG can provide, and speedy implementation will help meet that demand as well as provide timely proof of the success of the CBGP.