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Assistant Secretary for Financial Institutions Michael S. Barr Written Testimony before the House Financial Services Committee

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U.S. DEPARTMENT OF THE TREASURY

Press Center

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"Community Development Financial Institutions (CDFIs): Their Unique Role and Challenges Serving Lower-Income, Underserved and Minority Communities"

Chairman Frank, Ranking Member Bachus, this Committee has a long and bipartisan history of support for Community Development Financial Institutions (CDFIs). I want to thank you for the opportunity to testify today about the role of CDFIs in growing small businesses, creating jobs, and assisting economic recovery in distressed communities across the United States.

As we emerge from the worst economic crisis in generations, the Administration is focused on spurring greater job growth and ensuring that the recovery is firmly established. We still face an unemployment rate that remains unacceptably high, and credit is tight for small businesses and hard hit communities. Many families are struggling, and we must do everything we can prudently do to help.

As we seek an economic recovery that reaches communities across America, CDFIs are a critically important piece of our broader commitment to an inclusive recovery. CDFIs provide capital, credit, and financial services to hard-to-reach communities and underserved populations. In both rural and urban America, CDFIs are assisting the entrepreneurs and small businesses that are vital engines of economic growth.

CDFIs are able to reach low-income populations that have often traditionally lacked access to mainstream lenders. CDFIs also help bring mainstream financial institutions to these markets, for example through participating in loans with, or co-investing with, mainstream lenders. In this way, CDFIs serve as a bridge to the financial mainstream for their borrowers. CDFIs have helped finance small businesses, build charter schools, create homeownership opportunities, and support community health and child care centers. In short, CDFIs help finance our communities and revitalize our neighborhoods.

In today's economic climate, CDFIs' support to businesses, in particular small businesses, is more critical than ever. Looking back, CDFIs reported providing financing to over 10,000 businesses and over 1,600 commercial real estate properties in 2008. CDFIs also reported that they helped create or maintain over 70,000 full-time jobs in that period. [1]

Look's Gourmet Food Company in Whiting, Maine is a good example of the potential for CDFIs to facilitate small business growth and job creation. Look's had been a struggling company with just $800,000 of annual sales and 7 employees in 2002 in a coastal town of just 2,200 people. With a loan from the CDFI Coastal Enterprises, Inc. a local entrepreneur was able to buy the company in 2003 and expand its operations. Coastal Enterprises also provided the borrower with technical assistance in branding and marketing Look's handcrafted, hand-packed specialty seafood. Today, the company has 26 employees and sells its products nationwide.

Now more than ever we need to support the continued growth and vitality of CDFIs. Even in times of robust economic growth, some communities remain underbanked and underinvested. Rural America often struggles with low bank penetration and higher cost financial services. Some communities lack historical relationships with financial institutions. Some loans are simply too small for private lenders to make. Finally, some borrowers lack the credit histories that are required for today's automated underwriting environment.

CDFIs are there to fill the gaps. They are able to reach these communities through innovative, responsible and affordable financial products and services. The CDFI Fund has successfully provided CDFIs with the necessary capital to spur innovation in the sector.

Take the example of one award recipient, the North Side Community Development Credit Union, which serves low income populations on Chicago's north east side. North Side has developed an affordable small-dollar consumer loan for its customers. As of 2010, North Side has made over 5,500 of these loans totaling over $2.8 million, and the product is self-sustaining for the Credit Union. These loans saved community residents over $5 million compared to the rates and fees of alternative products available in that community.

Additionally, the current economic environment has strained the resources of many CDFIs. CDFIs have seen a dramatic increase in requests for lending services. However, CDFIs have faced constraints in meeting that increased demand. Their primary funding sources--banks, foundations, and socially motivated investors--have all decreased funding available to community development lending. Furthermore, CDFIs have had to increase loan loss reserves to manage downturns in their markets and have also faced an increase in losses. Nonetheless the industry is eager to deploy capital to assist in the economic recovery.

We strongly believe that further support is needed for CDFIs to help distressed communities manage through the economic downturn and to continue to serve as important engines of innovation in financial services to these communities.

That is why the Obama Administration has committed to supporting the important work of CDFIs and other community development lenders. We have used a wide range of tools to support and expand the reach of CDFI lending and investing, including tax credits, direct investments, and technical assistance. And we will continue to work closely with CDFI stakeholders to promote the private sector and public sector innovations that have helped make their work possible.

We have already worked with you to increase support to CDFIs through the Recovery Act, enacted in the Administration's first month in office. The Fund awarded $98 million in financial assistance to 69 CDFIs, spread across 26 states and Puerto Rico. Within 100 days of enactment of the Recovery Act, the CDFI Fund announced these awards, and within 60 days after that, disbursed 100 percent of the Recovery Act awards. The Act also provided us with an additional $1.5 billion in New Markets Tax Credit (NMTC) authority for both FY 2008 and FY 2009.

Given the strains placed on CDFIs by the financial crisis, and the congressional directives under the Emergency Economic Stabilization Act, we are extending low cost capital to CDFI depositories and holding companies, including banks, thrifts, and credit unions, through the new Community Development Capital Initiative (CDCI). CDFI depositories and holding companies are eligible to receive capital investments at a dividend rate of 2%. The CDFIs may receive investments up to 5% of risk weighted assets (or an equivalent amount of total assets for credit unions) through the CDCI. Consistent with prior capital purchase programs and the goals of promoting financial stability and protecting the taxpayer, CDFIs must apply to and be recommended by their primary federal regulator to participate in this program. The CDCI broadens eligibility for participation by providing that Treasury investment capital, when matched dollar-for-dollar by private capital, can be considered in the determination made by the institution's primary regulator.

As we begin to emerge from the financial crisis, our nation's distressed communities and the CDFIs that serve them will likely continue to lag behind in growth. That is why it is so important to bolster the CDFI field's capacity in the FY2011 budget. We have asked for increased appropriations to the CDFI Fund, strong levels of funding for the NMTC, and new initiatives for the CDFI Fund to help meet new challenges.

The President's FY 2011 Budget request of $250 million includes $140 million--a 30 percent increase--in funding for the Fund's financial and technical assistance awards to expand the availability of affordable capital in distressed communities. We have also requested $12 million in targeted funding to further CDFIs' work in Native communities.

While not proposing funding this year for the Capital Magnet Fund and the Bank Enterprise Awards, we have proposed two new initiatives, Bank on USA and the Healthy Food Financing Initiative

The Budget requests $50 million for "Bank on USA," which will promote financial education, broader access to bank accounts, basic credit products, and other financial services to help families meet their financial needs and build savings and solid credit histories. The program will build on and supplement community-based efforts involving state and local governments, non-profits, and a wide array of financial institutions, including CDFIs. In addition, this initiative will promote much needed private sector innovation in the field of consumer finance for low and moderate income households lacking adequate financial access.

The Budget also requests funding for CDFI's participation in a new multi-agency effort, the Healthy Food Financing Initiative (HFFI). The initiative will help to provide financing to increase the availability of affordable, healthy foods in underserved urban and rural communities. The Initiative brings Treasury together with the Departments of Agriculture and Health and Human Services to provide over $400 million in financing to organizations with sound strategies for addressing the healthy food needs of communities. These organizations will use the funding to attract private sector capital for investments to increase access to fresh produce and other healthy foods. Treasury will devote $250 million of NMTC authority and $25 million in CDFI Fund financial and technical assistance awards to this initiative.

In addition we are requesting an extension of New Markets Tax Credit authority and important reforms to the tax credit. This year, we requested $5 billion in NMTC authority for both 2010 and 2011. NMTCs have been able to leverage approximately $12 of private investment for every $1 of tax revenue foregone. To date, NMTC recipients have invested over $15.6 billion in distressed communities across the country. We are now proposing reforms that will help attract new investors, including allowing taxpayers to claim NMTCs against alternative minimum tax (AMT) liability, bringing the credit on par with the Low Income Housing Tax Credit. Allowing the credit to offset the AMT will enable this tool to attract even more private investors and help to speed recovery in the hardest hit communities . We are also working with the IRS on additional revisions to facilitate investments in small business that are the lifeblood of our communities.

Let me close by reiterating that Treasury is committed to supporting the CDFI Fund's work to help distressed communities weather the economic downturn and to support an economic recovery that reaches all Americans. We look forward to working with this committee further to strengthen the role CDFIs can play in recovery efforts and to help CDFIs continue to serve as pioneers in financial services to underserved communities.

Thank you.

[1] This data came from information reported to the CDFI Fund through their Community Investment Impact System in 2009. The reporting CDFIs were those who received CDFI Fund awards in the 2005-2008 funding cycles and they were reporting on their 2008 performance.