

**Final and Approved
CDFI Certification Recommendations
presented by the
Community Development Advisory Board
to
CDFI Fund Director Jodie Harris
August 27, 2020**

BACKGROUND

The Community Development Advisory Board (CDAB) occasionally creates subcommittees to gather and present information to the CDAB so that it can then advise the CDFI Fund on policy and program recommendations.

This subcommittee was formed on August 23, 2018 to review and comment on changes proposed by the CDFI Fund to modernize its CDFI Certification policies and reporting requirements. The criteria and measurements for certifying organizations as CDFIs have not been updated since the CDFI Fund was established in 1994. During this time, the CDFI industry has grown and evolved. In order to ensure certification criteria support the growth and reach of CDFIs, foster a diversity of CDFI types, minimize regulatory burden and safeguard CDFI Certification status, the CDFI Fund began reviewing CDFI Certification policies and tests applied to organizations seeking to become recognized as CDFIs in 2016.

Since its formation, the subcommittee has convened four meetings. It has formulated its positions and recommendations based on information gathered from CDFI Fund staff presentations, its review of the formal 'Requests for Public Comment' notices published by the CDFI Fund in the Federal Register, and from the individual experience and expertise of the subcommittee members for which they were appointed to the CDAB.

In accordance with the Federal Advisory Committee Act, all information gathered and developed by the Subcommittee will be presented to the full CDAB for consideration and deliberation. Approved recommendations will then be presented as advice by the CDAB to the Director of the CDFI Fund. The Subcommittee itself has not provided advice to the CDFI Fund directly.

RECOMMENDATIONS

The subcommittee would like to first recognize the diligent efforts of the CDFI Fund since the creation of this subcommittee that resulted in the publishing of Requests for Public Comment in

the Federal register related to a revised CDFI Certification Application and two Certification reports – the Annual Certification and Data Collection Report, and new Certification Transaction Level Report.

The subcommittee had extensive discussion regarding the nine sections of proposed changes associated with CDFI Certification policies and the tests applied to organizations seeking to become recognized as CDFIs. There were six primary areas the Subcommittee focused on during our time together. There were a number of other areas that we did note as potentially significant but did not rise to the level of recommendations to the Community Development Advisory Board for consideration.

PRIMARY MISSION

The area with the most conversation was related to Primary Mission of the applicant for certification. The unanimous opinion of the subcommittee is that the CDFI Fund staff was appropriately focused on ensuring applicants for CDFI Certification and all affiliates should have as a primary mission community development, meaning an applicant for certification, and its affiliates activities, are purposefully directed toward improving the social and/or economic conditions of underserved people and/or residents of economically distressed communities.

The CDFI Fund is proposing to enhance the tests it utilizes to verify that the Applicant's Financial Products and Financial Services align with its community development mission. This enhancement will require Applicants to provide additional information to allow the CDFI Fund to determine the adherence to community development mission.

Four main areas are discussed below regarding these enhancements.

- 1) Documenting a community development mission: Demonstrating acceptable community development mission for at least 12 months prior to application.
- 2) Alignment with Community Development strategy: demonstrating a community development mission and strategy of providing financial products and financial services to distressed and underserved communities and/or populations.

The Subcommittee strongly supported these enhancements to the application process to further ensure the integrity of the CDFI brand.

- 3) Responsible financing practices: An applicant must show financial products and services do not harm consumers by demonstrating affordability and the ability to repay along with fair collection processes in compliance with federal and state laws.

The subcommittee was in agreement with the increased level of discovery the CDFI Fund would take regarding products offered by Applicants. Several members expressed some concern regarding question P.M. 17.3 in the application which sets a fixed 5% default rate for a specific product. It was noted that some products by their nature have higher default rates and economic uncertainties, such as pandemics, can cause fluctuations in

default rates, so potentially a default rate over time might be a better measure. It was also discussed that the CDFI Fund might consider different default measures for different products as well. Members of the subcommittee suggested the CDFI Fund consider other ways to measure default rates other than a set percentage at a set time.

- 4) Affiliates: The CDFI Fund is proposing to expand the reporting of affiliates in the application and ensuring that all affiliated entities have a primary mission of community development, except if the parent or Affiliate is a tribal government. (This expands a requirement already placed on Depository Institutions Holding Companies.)

The Subcommittee discussed and agreed that the language should be expanded to include the exemption for Alaskan Native and Native Hawaiian CDFI Applicants to provide them the same treatment as Affiliates of tribal governments.

Additionally, the Subcommittee discussed the expansion of this section to revolving loan fund CDFIs. While in general agreement with the need to understand all the Affiliates associated with an Applicant, this criteria to require that the primary mission of the Applicant and all Affiliates to be community development could pose challenges for some already certified CDFIs, but could also potentially limit CDFI future activities. The subcommittee would request that the CDFI Fund ensure Affiliates of applicants that are providing Financial Products and Financial Services have a primarily mission of community development realizing some CDFIs may have Affiliates that do not provide Financial Products or Financial Services as the CDFI Fund defines them, and we would not want those activities to be tempered.

TARGET MARKET

The proposal that eligible target market activity no longer be limited to specific maps or strict geographic boundaries was supported as a way for CDFIs to provide Financial Products and Financial Services to a wider segment of the communities across the country as service channels have changes over the last 25 years, and restricting to geographic boundaries may reduce access to CDFI Financial Product and Financial Services in areas of need.

The Subcommittee spent significant time regarding two related areas.

- 1) First, how regulated institutions could meet the target market test by using not just the Financial Products test of 60% but also a combination of Financial Services and Financial Products. The CDFI Fund is recommending that if the depository institution has at least 60% of its Financial Services and at least 50% of its Financial Products to the target market it could receive CDFI certification and re-certification. In general, the Subcommittee understood this proposal as an effort to align the CDFI Fund's authorizing legislation with the CDFI Program regulations. This specific topic was discussed and resulted in both an understanding of the need for it but a desire for a higher threshold for Financial Products than the proposed 50%.

It was recommended that at least a “majority” of Financial Products should be in the target market and while 60% would defeat the purpose of creating the Financial Services and Financial Products option a higher level should be considered. The subcommittee could not gain consensus on a higher percentage.

- 2) Regarding the compliance period for existing Certified CDFI, having compliance assessed based on a three-year average for Financial Products closed and for regulated entities, Financial Services (depository accounts) provided through the last day of their most recent completed fiscal year provides for the management of a Certified CDFI to navigate through potential cycles of activity and helps to ensure CDFI certification is retained or lost when mission and strategy no longer meet CDFI certification criteria. This also supports the CDFI Fund’s elimination of its current policy of providing exceptions to Target Market threshold requirements and when combined with the ability to serve outside of a geographic target market should allow for consistent application of CDFI Target Market rules.

ACCOUNTABILITY – TARGET MARKET REPRESENTATION

The subcommittee is supportive of the CDFI Fund’s proposal of 33% of governing board be accountable to the proposed Target market with at least one governing board member being accountable for each Target Market.

The Subcommittee is strongly supportive of the enhanced requirements for an Advisory Board member to also sit on the Governing Board. Members of the Subcommittee also supported this proposal as it allows for CDFIs to further broaden board membership to include those with experience in lending, finance, accounting, and technology as CDFIs get more sophisticated.

There was concern regarding larger geographic coverage CDFIs not having as much contact with their geographic target markets but understood the tradeoff between local representation and the ability to serve larger geographies. The subcommittee believed the need to allow for CDFIs using new technologies to serve larger geographies to ensure access to CDFI Financial Products and Financial Services was reasonable.

NATIVE CDFI DESIGNATION

The subcommittee supported the expanded use of the term “Native Community” to include American Indian, Alaska Native or Native Hawaiian. Secondly, the subcommittee strongly supported the strengthening of the board and advisory board requirements to be certified as a “native CDFI.” Specifically, the requirements for membership and advisory board membership composition from the Native Community is fully supported.