December 29, 2020

The Honorable Steven Mnuchin
Secretary
United States Department of the Treasury
1500 Pennsylvania Avenue
Washington, D.C. 20220

Re: H.R. 133 - Consolidated Appropriations Act, 2021 – CDFI and MDI "Emergency Capital Investment Fund'

Dear Secretary Mnuchin:

On behalf of the members of the Community Development Bankers Association (CDBA) and the National Bankers Association (NBA), we respectfully submit the following recommendations regarding the Department of the Treasury's (Treasury) implementation of H.R. 133, Division N "Additional Coronavirus Response and Relief", which will establish a program to provide "Capital Investments for Neighborhoods Disproportionately Impacted by the COVID-19 Pandemic[1]" (the Capital Investment Program).

CDBA is the national trade association for banks and thrifts that are US Treasury-designated Community Development Financial Institutions (CDFIs). Our members have a primary mission of promoting community development and target at least 60% of their total lending and activities to Low- and Moderate-Income (LMI) communities and customers that are underserved by traditional financial service providers. Our members represent more than half of all CDFI banks, thrifts, and bank holding companies eligible to participate in the Capital Investment Program which is designed to ensure the economic recovery extends to all corners of the economy, particularly low-income and minority communities.

The NBA is the leading trade association for the country's Minority Depository Institutions (MDIs). Our mission is to serve as an advocate for the nation's MDIs on all legislative and regulatory matters concerning and affecting our member institutions as well as the

[1] H.R. 133, Division N, Title V, Subtitle B, Sec. 522 inserts a new section (Sec. 104, Capital Investments for Neighborhoods Disproportionately Impacted by the COVID-19 Pandemic) into The Community Development Banking and Financial Institutions Act of 1994 (12 U.S.C. 4701 et seq.)

communities they serve. Section 308 of the Financial Institutions Reform, Recovery and Enforcement Act of 1989 established several goals related to encouraging, assisting, and preserving minority depository institutions, including specifically charging Treasury and the Federal bank regulators with this obligation.[2] Many of our member institutions are also CDFIs and have historically been the only banks for consumers and businesses who are underserved by traditional banks and financial service providers.

The Capital Investment Program has great potential. The program's success will depend, in large part, on the effectiveness of implementation. The proposed program provides $9 billion in emergency Treasury capital investments in CDFI and MDI banks and their holding companies to support lending in low-income and underserved minority communities that have been disproportionately impacted by the economic effects of the COVID-19 pandemic. We believe that these institutions, which have each been recognized by Congress for their unique roles in LMI and minority communities, should be prioritized in this program.

Appropriately structured equity investments and subordinated debt can be the most powerful forms of capital that a CDFI bank or MDI can receive. Long-term, patient equity capital from partners – like the Treasury Department – can have a direct and catalytic effect on a financial institution's capacity to serve customers and communities that need it most.

Such capital can also be transformational in helping these institutions attract private sector capital that multiplies the positive effect of Federal investment. CDFI and MDI banks leverage this capital to grow loans and investments to targeted underserved communities. To be successful, the Capital Investment Program implementation needs to be quick, simple and flexible to allow CDFI and MDI banks to meet the needs of diverse urban, rural and Native American markets. Imposing cumbersome and unnecessary restrictions, where a nimble approach is needed, will only diminish the benefits, add costs, reduce dollars going to communities, and deter participation. LMI and minority communities have borne the brunt of the COVID-19 induced recession and priority should be placed on maximizing the participation of eligible financial institutions.

**Congressional Purpose**

In establishing the Capital Investment Program, Congress intended to empower CDFI and MDI banks to revitalize COVID-19 impacted LMI and minority communities. Thus, the Capital Investment Program is intended to be long-term, proactive and stimulative. This differs widely from the last time the Federal Government provided emergency equity to banks when it launched the TARP and CDCI Programs in the wake of the global financial crisis. TARP and CDCI were narrowly targeted at stabilizing the financial sector and lenders themselves. As such, the TARP and CDFI interventions were designed to be temporary with limited focus on the outcomes produced within the impacted communities.

[2] Financial Institutions Reform, Recovery, and Enforcement Act of 1989, Pub. L. No. 101-73, 103 Stat. 183 (1989)

**In rolling out this program, we strongly urge the Treasury Department to clearly communicate to all stakeholders and to the public that the purpose of the Capital Investment Program is very different than the TARP or CDCI Programs.** The TARP programs had a strong negative stigma as a "bail out" program for troubled institutions. The CDFI and MDI banks are in strong condition relative to the Great Recession. They do not wish participation in the Capital Investment Program to infer their banks are troubled or not well managed. To encourage participation, Treasury needs to ensure that communication on the program to external stakeholders is focused on the benefits CDFIs and MDIs create for low- and moderate-income and minority communities.

The differences in the Capital Investment Program intent language illustrate this essential distinction. (Emphasis CDBA/NBA).

| Capital Investment Program Authorization – *Division N, Title V, Subtitle B, Community Development Investment, Sec. 520. Purpose* | TARP Authorization - *12. USC 52, Emergency Economic Stabilization, Section 5201. Purposes* |
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| "The purpose of this subtitle is to establish emergency programs ***to revitalize and provide long-term financial products and service availability for, and provide investments in, low- and moderate-income and minority communities that have disproportionately suffered from the impacts of the COVID–19 pandemic***." | "The purposes of this chapter are - (1) to immediately provide authority and facilities that the Secretary of the Treasury can use ***to restore liquidity and stability to the financial system of the United States***; and (2) to ensure that such authority and such facilities are used in a manner that— (A) protects home values, college funds, retirement accounts, and life savings; (B) preserves homeownership and promotes jobs and economic growth; (C) maximizes overall returns to the taxpayers of the United States; and (D) provides public accountability for the exercise of such authority." |

Unlike during the Great Recession, financial institutions are generally healthy and well capitalized today. Congress intended the Capital Investment Program for healthy institutions to expand their work and contribute to a deep and wide economic recovery for underserved Americans by providing financial products and services at a greater scale than would be possible without it. It is critically important to note that infusions from the Capital Investment Program will help make participants an even greater source of strength and stability within their communities than ever before.

**Executive Compensation, Share Buybacks and Dividend Payments**

Within the Capital Investment Program's congressionally mandated purpose, we urge you to ensure that any regulations or restrictions on participating institutions be constructed to support the Program's intent. While we fully understand the strict statutory deadline under which the agency must issue an application and rules, **we strongly urge the Treasury to solicit industry comments on program components such as term sheets, regulations or other guidance prior to finalization.** CDBA and NBA have a series of recommendations that are important to maximize participation and ensure the Capital Investment Program achieves its public policy goals.

Under subsection (h), the Secretary is directed:

> "Not later than the end of the 30-day period beginning on the date of enactment of this section, the Secretary shall issue rules setting restrictions on executive compensation, share buybacks, and dividend payments for recipients of capital investments under the Capital Investment Program.[3]"

We are particularly concerned that this provision be implemented in a manner that does not undermine the long-term financial and operating viability of recipients. In the case of TARP and CDCI, which were focused on immediate stabilization of the financial services sectors, these provisions were implemented in a highly restrictive and punitive manner. They were structured to incent quick repayment and exit from the program as soon as an institution was able. The unintended consequence was that the program reduced the operating effectiveness for participating banks – such as reducing the ability of institutions to attract high-quality talent to replace departed senior officers.

The Capital Investment Program has a long-term focus and seeks to expand the capacity of CDFI and MDI banks to serve low-income and minority communities. **To accomplish this goal, we recommend the regulations reflect a balanced approach of safeguarding Federal resources while building the capacity of recipient institutions to serve their target markets.** Failure to take a balanced approach will discourage participation in the Program or undermine the viability of participating institutions. Both such outcomes ultimately harm LMI and minority communities. To be successful, the Capital Investment Program's regulations should recognize the distinct needs of CDFI and MDI banks. The regulations do not need to be complex. But, they should be flexible and encourage institutions to grow so they can continue to fulfill their community development missions.

[3] Division N, Title V, Subtitle B, Sec. 522(a)(h)(10)

Executive Compensation: Participating institutions must be able attract high quality talent. The work of CDFI and MDI banks is difficult and requires highly skilled management. Thus, the executive compensation restrictions of TARP and CDCI are wholly inappropriate for the Capital Investment Program and should not be adopted as they created barriers to attracting and retaining high quality talent. As a long-term, catalytic initiative, any rules should enable recipients to build healthy and vibrant institutions.

**We recommend that executive compensation regulations simply require recipients to report salaries and total compensation for the Chief Executive and C-level executives.** If a recipient institution is not in compliance with the terms of the Capital Investment Program, Treasury should have the right to limit excessive compensation that is not aligned with industry norms. For cases when a Capital Investment Program participant is not in compliance with the terms of its participation in the Program, (e.g. delays in the payment of preferred dividends or interest payments), *and* negligence is suspected, Treasury could sparingly impose limits on payment of executive level bonuses or freeze annual compensation levels until the noncompliance is cured. Under no circumstances should Treasury impose any clawback provisions on bank management and employees. As finding and retaining high quality senior leadership is critically important to the financial performance, regulatory compliance, and impact capacity of any CDFI or MDI, the terms and conditions of any Capital Investment Program monies should not deter or be a disincentive for any recipient to attract or retain high quality talent. Treasury's treatment of this issue will be critically important for incenting participation by the most financially strong and impactful CDFI and MDI banks.

Dividend Payments: Participating institutions must be able attract private capital over Treasury's anticipated long holding period. Having the ability to pay dividends is critical for attracting private capital; raising new capital is necessary to facilitate the financial health and growth of a CDFI or MDI bank. Thus, the dividend restrictions of TARP and CDCI are wholly inappropriate for the Capital Investment Program.

**We recommend that any regulations require recipients to simply report to Treasury on payment of dividends to shareholders. As a general rule, a well-capitalized institution should not face restrictions.** Yet, if a recipient institution is not in compliance with the terms of the Capital Investment Program, Treasury should have the right to limit excessive dividend payments that are not aligned with industry norms. Treasury should work with the banking regulatory agencies to obtain data on industry dividend payments for benchmarking. In the case of a Capital Investment participant that is not in compliance with the terms of its participation in the Program, (e.g. delays in the payment of preferred dividends or interest payments), Treasury could bar participants from paying dividends to other shareholders until the noncompliance is cured. To be noted, in the case of Sub S banks, Treasury should allow these institutions to distribute to shareholders the amounts needed to cover income taxes due given the specific tax requirements of this structure. Under no circumstances should dividend clawback provisions be imposed on investors.

Share Buybacks: Participating institutions must have the ability to manage their capital. To facilitate growth, some CDFI or MDI banks have developed mechanisms for providing limited capital liquidity. Other banks seeking to raise private capital may also choose to develop such mechanisms as part of their capital plans. This liquidity – combined with the ability to pay regular dividends – is important for attracting impact capital and new investors. Lack of capital liquidity can significantly impair institutional viability as many investors will eventually desire some return of capital. Thus, the share buyback restrictions of TARP and CDCI are inappropriate for the Capital Investment Program. If a bank already has a share buyback mechanism established to manage liquidity or develops a mechanism as part of a regulator-approved capital plan, they should not be inhibited as long as they are in compliance with the Capital Investment Program.

**We recommend that any regulations simply require recipients to report to Treasury buyback activity from shareholders.** Only if a recipient is out of compliance with the terms of the Capital Investment Program should Treasury have the right to limit excessive repurchase of shares that are not aligned with industry norms for peer community banks. Treasury should work with the banking regulatory agencies to obtain data on industry share buybacks for benchmarking. In the case of a Capital Investment Program participant that is not in compliance with the terms of its participation in the Program (e.g. delays in the payment of preferred dividends or interest payments), Treasury could limit participants from redeeming shares of other shareholders in excess of current earnings until the noncompliance is cured.

**Application and Selection Process**

Application: **As part of the application, we recommend that the Treasury coordinate with the CDFI Fund to streamline the application process. To the maximum extent practicable, we recommend the Department utilize data that has already been collected as part of the CDFI certification process or annual grant reporting.** We are very concerned about subsection (d)(4)(A)(i), which could be interpreted to conflict with the reporting standards for certified CDFIs. Specifically, it requires that applicants:

> "…demonstrate that not less than 30 percent of lending of the applicant over the past two fiscal years was made directly to low- and moderate-income borrowers, to borrowers that create direct benefits for low- and moderate-income populations, to other target populations as defined the Fund, or any other combination thereof, as measured by the total number and dollar amount of loans."

**Given that CDFIs must meet the far higher standard of 60% of their lending being directed to eligible Target Markets, we recommend that Treasury "rely on documentation submitted by the applicant to the CDFI Fund as part of certification compliance reporting" as directed in subsection (d)(4)(B), in lieu of imposing new data collection requirements. We also recommend that the Treasury utilize definitions and piggyback on reporting systems already utilized by the CDFI Fund.**

Selection: **As part of the selection process, we recommend that the Treasury give highest priority to applicants that dedicate the highest proportion of their lending and services to any CDFI Fund eligible Target Market(s).** We are concerned that the alternative definition in subsection (d)(4)(A)(i), does not maximize benefits to the customers and communities that need it most with only a 30% threshold for historic performance in serving specified markets. As such, CDFIs should receive highest priority in the selection process, as it maximizes the programmatic use of taxpayers' dollars. To the extent that non-CDFIs can meet the 60% threshold, they should also receive priority but should be encouraged to become certified CDFIs. Likewise MDIs, which are specifically designated in the statute, and which Section 308 of FIRREA directs Treasury to preserve and promote, should also receive priority in the selection process based on the proportion of their service to CDFI eligible Target Markets.

**Nature of Investments**

To the maximum extent, in making investments into eligible institutions, the Treasury should structure the terms and conditions to maximize the ability of recipients to create benefits for customers and communities – which is consistent with the program's Congressional mandate. Above all, the Capital Investment Program should encourage mission-focused CDFI and MDI banks to grow and be profitable so they can maximize fulfillment of their community development missions and positively impact low- and moderate-income and minority communities.

It is important that any regulations recognize the important qualities of CDFI and MDI banks – they are for-profit institutions that must balance purpose and profit. All mission focused CDFI and most MDIs banks are small by any common financial services sector definition. Among certified CDFI banks, the largest is $5 billion in total assets and the sector's average size is $441 million in total assets. MDIs are far smaller than the average non-MDI bank. Compared to commercial banking institutions on average, they are very small; the largest institution has only $38 billion in total assets. Black and Hispanic MDIs have average assets of $245 million and $2.7 billion, respectively, compared to an average of $3.1 billion for all US banks. While a small handful of CDFI and MDI banks are publicly traded, most are privately held and generally closely held. Therefore, their capital structures are often illiquid, and the requirements of the banks for flexibility under the Program is crucial to their existence.

Treasury needs to recognize the different types of organizational and capitalization structures. Generally, CDFI and MDI banks are organized as either one of two types of corporate entity: C Corporations (C Corps) or Sub S Corporations (Sub S Corps). While the interests of banks in relation to the Capital Investment Program will vary beyond the requirements of their structure, we believe it is essential to recognize how corporate structure will influence their participation and the potential structure of investment instruments.

The statute clearly contemplates involvement of C Corps with the explicit authorization of issuance of preferred stock. We note that even C Corps may have an interest in utilizing some portion of capital in the form of subordinated debt depending on their capitalization needs. **We**

**urge the Treasury to allow applicants to request the mix of capital that is the best fit for their institutions.**

The statute appears to allow CDFI or MDI bank holding companies to be participants. We applaud and support this inclusion. **We recommend CDFI and MDI bank holding companies have the option to request either preferred stock or subordinated debt.** It is also important for Treasury to recognize that some institutions will prefer to apply and receive capital through their bank holding companies, while others will prefer to apply and receive capital through their banks. Thus, any investment instruments and term sheets should be structured to anticipate this variety.

**We urge Treasury to offer financial instruments suitable for Sub S banks as they cannot issue preferred stock.** They will need to utilize the subordinated debt option. S Corp structure has been historically adopted by, and remains emblematic of the closely held, or family owned, community bank. This structure is often used by both MDIs and rural banks. These banks and their customers are among those targeted by this program, and their participation is vital to the Capital Investment Program's success.

**Per subsection (f) we strongly urge Treasury to consult with regulators to ensure that its investment instruments meet the requirements for Tier 1 capital.** Reducing regulatory risk and uncertainty will encourage participation. In particular, we note that the term of any investment should be indefinite and the post-year 10 pricing should not trigger a change in regulatory treatment. An increase in dividend rates may be deemed by regulators as a forced liquidity mechanism and will prevent Tier 1 treatment. To ensure Tier 1 treatment, we strongly urge that noncumulative dividends be paid only if common shareholders receive dividends. Furthermore, Treasury's preferred stock should not be mandated to be the most senior to other preferred stock as it was with CDCI. During CDCI, such a provision inhibited banks from raising new private capital and will similarly inhibit CDFI and MDI banks from raising private capital needed to support future growth. Finally, per subsection (d)(6)(B)(i) we ask Treasury to ensure its offerings clearly reflect Congressional intent that absolutely no dividends, interest or other payments will be required or accrued for the first 24 months.

**We strongly urge the Treasury to consult with the regulatory agencies on all aspects of the effect this capital will have on supervisory activities.** For example, we note a long-standing Federal Reserve supervisory view that bank holding companies should have voting common equity as the "dominant" form of capital. While not formally stated as a rule for bank holding companies under $3 billion in total assets, this standard is generally applied to all bank holding companies as a safety and soundness practice. We note the Federal Reserve has sometimes discouraged use of instruments such as preferred stock, trust preferred securities, or non-voting common stock for fear of "over reliance." Thus, Capital Investment Program participation could subject an institution to supervisory criticism and severely discourage participation. Treasury can reduce this regulatory risk by proactively working with the regulatory agencies to ameliorate these concerns and ensure there is clear communication with the agencies and program participants on regulatory treatment. **Given the long-term nature of**

**the Capital Investment Program, we recommend that the Treasury work with the Federal Reserve to ensure its instrument and similar private capital instruments directed at CDFI and MDI banks are exempted from this calculation.** Such treatment will enable participants to attract greater amounts of private capital, which will expand access to capital with target communities intended to benefit from the program.

Other subjects of concern which require clear guidance include, but are not limited to:

- Risk-Based Capital Rules governing the definition of conservative capital buffers;
- Prompt Corrective Action Rules by which FDIC insured institutions are subject to tiered minimum capital requirements;
- The Community Bank Leverage Ratio whereby banks with less than $10 billion assets may elect to comply with regulatory capital rules by holding a ratio of Tier 1 capital in excess of 9%;
- The Small Bank Holding Company Policy Statement whereby the Federal Reserve generally does not require compliance with the Risk-Based Capital Rules for Bank Holding Companies (BHCs) that have less than $3 billion in consolidated assets;
- Federal Reserve Control Rules whereby the Federal Reserve considers “control” to be determined based upon a range of factors and has rules that govern, for example, a determination as to whether an investor is deemed to be a bank or savings and loan holding company.

**We strongly urge Treasury to clarify that CDFIs and MDIs have the option, at their choice, to trigger a buyback, sale or transfer, or redemption of Treasury’s preferred investment at any time. We also urge Treasury to provide guidance on how the option to sell or transfer the investment to a mission-aligned affiliate nonprofit will be executed.** This guidance in particular should be developed in close consultation with the industry leader advisory council proposed below.

If deemed permissible under the statute and feasible, **we also urge the agency to consider the adoption of the option for participating institutions to draw down investments in tranches prior to the conclusion of the 6-month period required for Treasury to complete its investments.**

**Restrictions**

As the pandemic has affected LMI communities nationwide, **we urge the Treasury to maximize participation among eligible mission focused CDFIs and MDIs.** Subsection (e) gives the Treasury the authority to make very large investments relative to total bank asset size. Yet, we urge the Treasury to consider making investments in amounts that ensure geographic diversity among interested CDFIs and MDIs. Investment decisions should balance future potential growth with deployment capacity. In the event the Treasury has allocated capital to institutions described under any of the Set Asides and still has additional capital available, we urge you to make that capital available among other institutions.

## Ineligible Institutions

Section 104A(i), states that: *"An institution shall be ineligible to participate in the Program if such institution is designated in Troubled Condition by the appropriate Federal banking agency or the National Credit Union Administration, as applicable, or is subject to a formal enforcement action with its primary Federal regulator that addresses unsafe or unsound lending practices."* This is potentially in conflict with an earlier clause, Section 104(A)(d)(2), which requires the Secretary to consult with regulators to determine eligibility.

**We urge Treasury to defer to the bank regulatory agencies in determining a bank's eligibility for consideration.** This would allow the regulator to work with a bank under a formal enforcement action around lending practices to put guard rails in place to allow the bank to gain access to the desperately needed capital, while at the same time protecting the government's interests. For example, the bank could show in its application and deployment plan how it would not only use the capital to make additional loans in the community, but also be able to re-direct other resources towards talent or technology to address underlying challenges in compliance or lending practices. In our experience, access to additional capital usually solves regulatory issues, because small banks often need it to access additional internal resources. Lack of these resources makes it challenging to address safety and soundness concerns. Treasury should work with the regulators and exercise maximum discretion to allow CDFI and MDI banks to fulfill Congressional intent to get capital in the hands of LMI and minority communities.

## Collection of Data

Subsection (k) provides eligible institutions with greater authority, if they choose, to collect demographic data on customers otherwise prohibited under the Equal Credit Opportunity Act (ECOA). This authority is critically important for CDFI banks and MDIs to increase service to minority and other underserved communities. **We encourage Treasury to work with the regulatory agencies to ensure examiners fully understand this authority.**

## Reducing Payments

Under subsections (d)(6)(B)(ii)-(iii), **we urge the Treasury to clarify how increases in lending activities will be measured for the purpose of qualifying for reduced payments.** For example, will the increases be measured based on overall increases, or specifically on increased lending to borrowers that create direct benefits for low- and moderate-income populations per subsection 4 (i.e., loans to businesses that provide jobs and/or services to low- or moderate-income individuals)? Clear guidance on metrics and definitions will help participants set up systems for tracking and measuring their activities. We urge Treasury to publish a proposed rule for public comment prior to implementation.

**Advisory Panel of CDFI and MDI Leaders to Advise on Implementation**

We recognize that our comments, and those of colleagues at shared-interest trades, cannot provide a comprehensive list of suggestions within the bounds of a single letter. **We strongly urge the Treasury to convene a representative panel of CDFI and MDI trade leaders and practitioners to provide insight on the development of guidelines for implementation**.

In conclusion, the membership of CDBA and NBA fully appreciates the thoughtful consideration of the Treasury and its staff as the Capital Investment Program is implemented. This is a wonderful opportunity to expand the positive influence of a long-standing market-based solution within COVID-impacted communities, and we sincerely appreciate the opportunity to comment and offer feedback. We look forward to future discussion on these important issues.

If you have any questions, please contact Jeannine Jacokes, CDBA Chief Executive Officer, at (202) 689-8935 ext. 222 or *jacokesj@pcgloanfund.org*, or Robert E. James, II, NBA Chairman, at (912) 447-4217 or *rjamesii@carverstatebank.com*.

Sincerely,

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| Jeannine Jacokes | Robert James, II |
| Chief Executive Officer | Chairman |
| Community Development Bankers Association | National Bankers Association |