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Via Electronic Submission

The Honorable Janet Yellen
Secretary
United States Department of the Treasury
1500 Pennsylvania Avenue
Washington, DC 20220

RE: Emergency Capital Investment Program – Restrictions on Executive Compensation, Share Buybacks, and Dividends; TREAS-DO-2021-0004; RIN 1505-AC76

Dear Secretary Yellen:

The members of the Community Development Bankers Association (CDBA) respectfully submit the enclosed comments in response to the interim final rule (IFR) request for comments related to the Department of the Treasury's (Treasury's) implementation of the Emergency Capital Investment Program (ECIP).

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 ECIP which is designed to ensure the economic recovery extends to all corners of the economy, particularly low-income and minority communities.

CDBA believes that ECIP has the great potential to catalyze the next phase of growth and development for depository Community Development Financial Institutions (CDFIs) and the communities and customers they serve. These communities have been disproportionately impacted by the economic effects of the COVID-19 pandemic and long term structural inequities of low income and communities-of-color.

We are excited about the opportunity to work with Treasury to make ECIP a success. ECIP's success will depend, in large part, on the effectiveness of implementation. To achieve the program objectives set forth by Congress, Treasury will need to ensure ECIP reaches a broad range of eligible institutions and there is robust industry participation. We strongly encourage the agency to engage in active outreach to all eligible institutions. Among the most important elements of education will be differentiating ECIP from Treasury's Great Recession era's Troubled Asset Relief Program (TARP) and the Community Development Capital Initiative (CDCI). Many eligible institutions participated in these programs and had a negative experience given the inflexibility of the authorizing statute, constantly changing rules, and negative public perceptions.

We believe the ECIP statute has a strikingly different purpose, tone, and provides the agency with significant latitude in implementation that can facilitate the growth of the depository CDFI sector. **Whether Treasury achieves this outcome will depend on the effectiveness of its communication strategy, its willingness to protect program participants from potential changes in the policy environment, and the flexibility of the agency to ensure the program is applied in a manner that fits individual program participants and their communities.** We believe the Treasury should look to the lessons learned over the past quarter century by the CDFI Fund in implementing programs for a diverse CDFI sector in a fair and equitable manner.

COMMUNICATION: We recommend that the Treasury issue clear, written communication about how ECIP is different than TARP and CDCI with respect to Executive Compensation, payment of dividends, and stock buy backs. In particular, the agency should explicitly inform applicants that as long as these policies and practices are in conformance with the requirements of the applicants' primary regulatory agencies, they will satisfy the ECIP requirements. Likewise, the Treasury should explicitly inform applicants that as long as their policies and practices with regard to "excessive or luxury expenditures" are in conformance with the requirements of the applicants' primary regulatory agencies, they will satisfy ECIP's requirements. Such communication will mitigate concerns of a duplicative and potentially conflicting set of parallel requirements.

SHIFTING POLICY PRIORITIES: CDBA is grateful for the strong support demonstrated by Congress and the Biden Administration for CDFIs. We believe the current Administration is well-aligned with supporting CDFIs and MDIs. Political winds, however, will likely change over the period in which Treasury holds ECIP investments. We strongly urge Treasury to contractually lock the program terms, conditions, and requirements into the ECIP investment documents to protect program participants. During TARP and CDCI, negative public sentiment about the programs contributed to an ever-shifting set of program rules and agency direction. Constantly shifting rules create significant operations risk for recipient institutions. To address this risk, CDBA recommends Treasury commit to contractually binding the agency to the terms, conditions, and program requirements outlined in the investment documents. Any changes to the documents can only occur with the consent of all parties to the transaction. We believe such a commitment will encourage more eligible CDFIs and MDIs to participate in the program.

DISPOSITION: We strongly urge Treasury to set clear guidelines related to the eventual disposition of its holdings prior to the application deadline. Questions around disposition are critical to CDFI banks' decision to apply to ECIP. Failure to address this issue will greatly suppress interest in the program. Applicants want to understand what they are committing to before agreeing to participate in ECIP. The ECIP application materials published to date create great uncertainty as to whether Treasury intends to be a patient investor -- implying that it may -- or will -- dispose of its holding after 10 years. In the context of bank equity capital, 10 years is a very short time. Most bank investors retain their holdings for decades. Given the anticipated dollar amount of ECIP investments, few or no banks will experience enough organic growth to buy back Treasury's holdings in 10 years. Thus, exactly like TARP, they will be faced with the threat that their stock will be sold on the market -- potentially to investors that do not share or value the mission or purpose of a CDFI or MDI. While only 25% of preferred nonvoting stock or a subordinated debenture can be sold to a single buyer, selling ECIP securities after 10 years places mission and/or minority status at grave risk. Numerous CDFI and MDI banks have dealt with activist investors that had no formal voting rights, but worked to influence other shareholders to change the direction of an institution.

To protect the mission-integrity of depository CDFIs and MDIs, the industry successfully advocated that Congress authorize Treasury to transfer or sell its interest for no consideration or for a de minimis amount to a mission-aligned nonprofit affiliate of the participating institution. This option is a valuable tool for protecting the long-term public interest of taxpayers. Through ECIP, taxpayers are supporting the work of depository CDFIs and MDIs to deliver credit and financial services to underserved people and places. Keeping ECIP-originated investments in the hands of parties that are aligned with the mission and purpose of CDFIs and MDIs, will preserve the important role these institutions play. Without such a provision, ECIP could inadvertently lead to the loss of many mission-focused financial institutions if non-mission aligned investors were to gain control.

REGULATORY COORDINATION: CDBA strongly urges Treasury to work closely with Federal regulatory agencies on ECIP implementation. The treatment of ECIP investments by the Federal Reserve Board (the Board), Federal Deposit Insurance Corporation (FDIC) and Office of the Comptroller (OCC) are critical to the success of the program. In the short term, we urge Treasury to work with these agencies to develop processes to ensure timely approval of ECIP applications. We strongly urge Treasury and the regulatory agencies to develop examiner training on ECIP to ensure support at headquarters filters down to the examiner level.

REGULATORY AGENCIES & ECIP TERM SHEET POLICY: We urge Treasury to engage the bank regulatory agencies' as they address critical questions raised by the draft term sheets outlined below. To be noted, CDBA will submit additional comments under separate cover pursuant to the IFR issued by the regulatory agencies.

1. ECIP's authorizing statute says that the maximum rate for both forms of capital is 2%.[1] The term sheet, however, states that Sub S and mutual banks receiving Subordinate Debt are subject to a maximum rate of 2.5%. The rate on both investments should adhere to the statutory maximum of 2%, without exception.
2. The statute states that sub debt should receive treatment consistent with the Tier 1 treatment for preferred stock.[2] Yet, the sub debt capital term sheet say it will be treated as Tier 2. Treasury must work with the agencies to ensure that capital treatment is consistent with the legislation. CDBA urges Treasury to ensure that the capital treatment on both investments should adhere to the statutory requirement for "consistency."
3. The C Corp term sheet allows for maturity perpetual, while the Sub S term sheet only allows capital to be available for 15 years. This treatment in the term sheet is not consistent with the statutory language. We urge Treasury to work with agencies to ensure that term sheets meet the statutory requirement that treatment of Sub S capital be "consistent with requirements . . . applicable to the terms of preferred stock issued by institutions participating in the program." The duration treatment of Sub debt is simply not "consistent" with that for preferred stock.
4. CDBA recommends the FDIC work within Prompt Corrective Action Rules (by which FDIC insured institutions are subject to tiered minimum capital requirements) to ensure that ECIP participation does not negatively influence the FDIC's enforcement of the rules.

[1] "No dividends, interest or other similar payments shall have a rate exceeding 2 percent per annum for the first 10 years."
[2] "Consistent with requirements . . . applicable to the terms of preferred stock issued by institutions participating in the program."

COMMENTS ON INTERIM FINAL RULE – RESTRICTIONS ON EXECUTIVE COMPENSATION, SHARE BUYBACKS & DIVIDENDS

RESTRICTIONS ON COMPENSATION & EXPENDITURES

Question: Are the restrictions on compensation sufficiently tailored to facilitate the ECIP Program objectives without discouraging participation in the program?

CDBA believes the restrictions on compensation are acceptable and should not discourage participation in the program. We believe that it is important for Treasury to defer to the bank regulatory agencies on the matters of policy, practice and compliance rather than create a new duplicative regulatory requirements. We applaud the IFR's deferral to existing regulatory guidelines or already widely adopted policies, as they pertain to:

> (A) Excessive compensation as articulated in the Interagency Guidelines Establishing Standards for Safety and Soundness;
> (B) Severance pay as articulated in FDIC rule 12 CFR part 359; and
> (C) Excessive or luxury expenditures as articulated in the template policy (which closely resembles those already adopted by many CDFI banks). This reliance on existing regulatory requirements enhances the transparency required for compliance and reduces redundancy.

We are, however, concerned about a potentially overbroad definition of "troubled institution" which is inherent in FDIC rule 12 CFR part 359. The IFR's restrictions include a "restriction on severance pay for an ECIP recipient's senior executive officers if the ECIP recipient is in troubled condition." We urge Treasury to work closely with the agencies to ensure they exercise maximum discretion regarding "Troubled Institutions" to allow CDFI and MDI banks to fulfill Congressional intent to get capital in the hands of LMI and minority communities.

We are concerned that the "Troubled Institution" definition extends the exclusion of institutions beyond those with truly troubled composite ratings or subject to serious cease and desist letters, to include those subject to a "written agreement" to "improve their financial condition."[3] This is potentially in conflict with a clause within the establishing statute, Section 104(A)(d)(2), <u>which requires the Treasury Secretary to consult with regulators to determine eligibility.</u> This requirement to consult with regulators should extend to the determination of "Troubled Institutions" for the purposes of determining any restrictions on compensation.

In the case of enforcement actions put in place over the course of the bank's participation in ECIP, we urge Treasury to work with the regulatory agencies to establish internal guard rails to allow banks to retain access to ECIP capital over the course of their participation in the program, while at the same time protecting the government's interests. Specifically, page 11 of Treasury's IFR, Section 4, "Annual Certification and Enforcement," mitigates the potential interference of new enforcement actions: "If an ECIP recipient certifies that it satisfies the severance payments requirements, Treasury expects that the (annual compliance) certification will address <u>only compliance with the requirements and will neither address whether the ECIP recipient is in troubled condition for purposes of 12 CFR parts 359 and 750, as applicable, nor contain any confidential supervisory information subject to applicable disclosure restrictions promulgated by the ECIP recipients' federal regulators</u>." This is a positive position, and should be a point reinforced independently by the bank regulatory agencies. These agencies should

[3] 12 CFR § 303.101 (c)(3) and (4)

apply discretion to their consideration of enforcement actions put in place over the course of a bank's ECIP program participation, in line with the intent of Treasury's statement.

Question: Are there other reasonable alternatives to the Program's excessive or luxury expenditures policy requirement that would be as effective in ensuring that funds provided under the Program are used to provide loans, grants, and forbearance, without restricting ECIP participant discretion to establish policies and procedures that are tailored to meet the needs and business objectives of their respective organizations?

CDBA believes the principles outlined in the IFR's Appendix A, "Model Excessive or Luxury Expenditures Policy" are acceptable given the needs and capacities of CDFI banks. We applaud Treasury's deferral to the regulatory agencies' approval of bank policy guidelines that are already widely adopted as a means of meeting the requirement.

Question. ***What additional guidance or clarification regarding the compensation and expenditure restrictions would help facilitate compliance with these restrictions and ensure that the restrictions are working as intended?***

Treasury should affirm that existing bank policies that are substantially similar to Treasury's model policy are sufficient for the purposes of ECIP. Compliance with the policy should be a matter of concern for the bank's primary regulators. Further, under no circumstances, should Treasury require any banks, with regulator-approved policies in place, to submit any activities for approval. To facilitate greater ECIP participation, CDBA recommends that Treasury develop and distribute an illustrative, non-comprehensive, list of examples of activities both considered "excessive" and "within bounds." We also urge Treasury to clarify that "Reasonable" expenses should be specifically construed to reflect that if a bank's primary regulators have approved a bank's policies and practices, it will suffice.

RESTRICTIONS ON DIVIDENDS, SHARE BUYBACKS AND OTHER CAPITAL DISTRIBUTIONS

Question: Are the restrictions on dividends, share buybacks, and other capital distributions sufficiently tailored to facilitate the ECIP Program objectives without discouraging participation in the program?

CDBA believes the restrictions on dividends, share buybacks and other capital distributions appear generally aligned with common industry practice and should not dissuade participation in ECIP. We applaud Treasury for deferring to the bank regulatory agencies on matters of policy, practice and compliance rather than creating new duplicative regulatory requirements.

CDBA does, however, have concerns about specific bank structures (S Corp and Mutual) that, if not addressed, may discourage participation in the program. While the proposed instrument appears appropriately structured to promote engagement by C Corp banks, the IFR is less encouraging for S Corps and Mutual Banks. CDBA strongly recommends that Treasury work with the Federal Reserve to ensure the Board modifies the Small Bank Holding Company Policy Statement (the Policy Statement) in connection with the IFR and create an exception under Section 2.C (Dividend restrictions). This exception should clearly state that Sub S Corp bank holding companies may exceed a 1.0:1 debt-to equity ratio and still issue dividends to cover Sub S Corp owners' tax obligations in respect of the Sub S Corps' earnings. Because Sub S Corp CDFI banks and MDIs are small organizations, keeping their debt-to-equity ratios at 1.0:1 will be impossible if CDFIs and MDIs apply for the amounts Congress authorized. If the Board does not allow banks to pay owners' tax obligations incurred in connection with the pass-

through entities earnings, virtually all owners will be forced to limit their capital application. The organizations closest to the underserved communities will be materially curtailed in their ability to apply for capital.

Providing such an exception would be consistent with the position the Board took with respect to the Temporary Asset Relief Program (TARP), established by the Emergency Economic Stabilization Act of 2008. At the time TARP was established, the Board amended Section 2.A of the Policy Statement to add language clarifying that:

> "Notwithstanding any other provision of this policy statement and for the purposes of compliance with paragraphs 2.C [Dividend Restrictions]… a bank holding company that has made a valid election to be taxed under Subchapter S…may exclude from debt subordinated debentures issued to the United States Department of the Treasury under [TARP]".

The Board should also amend the Policy Statement to add the ECIP, and maintain consistent treatment of subordinated debt issued by the Treasury. This approach, in concert with the ECIP IFR, will permit dividends to pay owners' tax obligations incurred in connection with the owners' earnings.

Question: What would be the advantages and disadvantages of aligning limitations on capital distributions under the interim final rule with limitations applicable to each entity pursuant to the requirements of its appropriate federal banking regulator? What are the advantages and disadvantages of calculating eligible distributable income based on (i) income as of the end of the most recent calendar quarter and (ii) year to date reported net income? What are the advantages and disadvantages of calculating the capital distribution limitation using (i) year-to-date dividends or capital distributions; (ii) reported dividends or capital distributions; and (iii) year-to-date dividends or capital distributions as of the end of the most recent calendar quarter?

Wherever possible, limitations on capital distributions under the IFR should align with limitations pursuant to the requirements of an ECIP participant's primary bank regulatory agency. We strongly urge Treasury to provide leadership as regulatory agencies consider and address concerns related to capital and distributions that require clear guidance. Specifically:

1. A Sub S bank that is well capitalized and current on its obligations to Treasury should be able to declare additional dividends above the normal "tax distribution."
2. Once an ECIP participant increases their Qualified Lending -- as compared to the Baseline -- to such an amount that the dividend rate will decrease, Treasury must clarify if and how the rate payable will be responsive to the qualified lending compared to the baseline over the course of the 10 year initial required hold period, and after.

The (dis)advantages of calculating eligible distributable income in the scenarios above will vary by bank. CDFI banks have widely varying business models and ownership structures, and based on their location and other external factors, they experience different business cycles (both seasonal/short- and long-term). While there is a clear difference between the time frames in the scenarios above, for some banks it might be more appropriate or advantageous to choose one scenario or the other. These calculations will resist attempts at generalization. We strongly urge Treasury to address this question on a case-by-case basis at a stage in the process when banks' eligibility has been determined so that their particular needs and those of their communities are met.

The (dis)advantages of calculating the capital distribution limitation in the scenarios above will also vary by bank and for similar reasons as above. For example, if a bank declares dividends at the end of the year, then YTD dividends would only be an issue for the 4th quarter and would be zero for the other quarters. Banks will have varying distribution schedules based on their ownership and performance, and again, these calculations will resist attempts at generalization. As above, we strongly urge Treasury to address this question on a case-by-case basis at a stage in the process when banks' eligibility has been determined so that their particular needs and those of their communities are met.

Conclusion

The membership of CDBA fully appreciates the efforts and thoughtful consideration of the Treasury and its staff to implement ECIP. As noted, we believe ECIP has the great potential to catalyze the next phase of growth and development for depository Community Development Financial Institutions (CDFIs) and improve the lives of residents and businesses of communities they serve. We are excited about the opportunity to work with Treasury to make ECIP a success.

If you have any questions, please contact Jeannine Jacokes, CDBA Chief Executive Officer, at (202) 207-8728 or *jacokesj@pcgloanfund.org*, or Brian Blake, CDBA Public Policy Director at (646) 283-7929 or *blakeb@pcgloanfund.org.*

Sincerely,

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