March 1, 2008

Christopher Stever
Certification and Training Manager
CDFI Fund
U.S. Department of Treasury
601 13th Street, NW, Suite 200 South
Washington, DC 20005

Dear Mr. Stever:

Opportunity Finance Network[1] appreciates the opportunity to address the CDFI Fund's Request for Comments published in the *Federal Register* on February 5, 2008. We value the longstanding partnership the CDFI Fund has had with the industry in certifying CDFIs, and offer comments that strive to continue that partnership.

Opportunity Finance Network has long advocated two principles:

- That certification not convey judgment about a CDFI's performance or suggest that it is a substitute for sound investor underwriting; and
- That the Fund respect CDFIs as market-driven institutions, and support individual CDFIs' decisions about their strategies and structures to serve those markets.

The request for comments indicates that the Fund is considering changes that could seriously undermine these two principles. Because Opportunity Finance Network and its members believe that certification in its current form has served the needs of the industry well, we strongly urge the Fund not to implement significant changes to the process.

We also are concerned that the Fund has provided only a short timeframe for feedback. The range of questions in this request for comments indicate that the Fund is considering a substantial overhaul of the certification process. It should provide the industry with more than 30 days to analyze, consider, and respond to such a dramatic shift.

We understand the Fund's desire to develop consistent standards for certification, and we applaud and support that effort. However, the variety of institutions comprising the CDFI industry makes the kind of "bright-line" decisions the Fund seems to be suggesting in its questions extremely difficult, if not impossible. It also appears that the resources the Fund would need to devote to the certification process to conduct the kind of review of each CDFI's products and services that it would need to make these determinations would far outstrip the staff time available. We would not support putting more resources into a process that could produce substantially less value for the CDFI industry.

Because our premise is that the certification process is essentially sound, OFN strongly recommends that the Fund leave its current certification practices unchanged. In addition, while our membership includes representation from the full spectrum of CDFI types, we urge the Fund to consider carefully the recommendations from associations representing specific sectors.

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[1] Opportunity Finance Network, the national network of more than 160 financial institutions creates growth that is good for communities, investors, individuals, and the economy. Its members include Community Development Financial Institutions (CDFIs) and other opportunity finance institutions that work just outside the margins of conventional finance to bring those markets into the economic mainstream and to help the economic mainstream flow into those markets. CDFI financing has resulted in significant numbers of new jobs, jobs preserved, quality, affordable housing units, and new commercial and community facility space in all 50 states. Over the past 30 years, the Opportunity Finance industry has provided more than $23 billion in financing that would not otherwise have happened in markets that conventional finance would not otherwise reach.

The Function of Certification for CDFIs

While certification is first and foremost the Fund's determination of eligibility for its programs, public and private investors have come to recognize it as a common description of an organization's function and purpose. While investors conduct their own underwriting and due diligence, many have used CDFI Fund certification as a screen to begin their decision making. The Fund should take pride in the role it has played in making "CDFI" a widely understood term in the investor community through its certification process.

Because the term "CDFI" has currency in its current form, the Fund should exercise extreme caution in making any significant changes, which risk confusing the CDFI marketplace. To ensure that their investment is used for its intended purpose, many CDFI investors have included in covenants that investees maintain status as CDFI Fund certified institutions. Some federal guidelines, including Community Reinvestment Act regulations, offer incentives for investment in certified CDFIs. To change certification requirements could mean that an institution that had previously qualified might find itself uncertified, and out of compliance with investor covenants.

As stated in our introduction, we share with the Fund a concern that certification not be mistaken for a judgment on a CDFI's effectiveness or viability. However, "CDFI certification" has an accepted definition in the opportunity finance community, generated by more than a decade of work and education by the Fund and the industry. The Fund should not take actions that threaten this common understanding.

Maintaining Flexibility in Certification

Because CDFI certification is not based on any tests of quality and does not confer to CDFIs a "seal of approval," the Fund should not presume to assess an individual CDFI's products, services, or strategies. A hallmark of the CDFI Fund's programs—what distinguishes it from other government programs—is its practice of investing in a CDFI's strategy, not in particular projects or practices. The Fund should continue to apply this principle of flexibility to its certification practices, in line with the purpose the Fund was created to fulfill. A detailed assessment of a CDFI's products and services, as the Fund seems to be considering, would run counter to the market-focused character of the CDFI industry.

The Fund has supported the development of a vibrant, varied CDFI industry by recognizing that CDFIs develop market-responsive ways to meet their missions. Generally, prescribing limits or specifics about pricing, services, or board makeup would undermine this longstanding commitment to supporting the full spectrum of CDFIs that, in turn, meet rapidly changing market needs.

In several instances, the Fund asks whether criteria ought to be applied differently to diverse types of CDFIs. While the Fund has made appropriate distinctions between depository and nondepository CDFIs in the award process, we caution the Fund against additional differences based on "category." Many CDFIs are hesitant to include themselves in only one category, offering many products in a multifaceted institution. Except in a few very specific circumstances outlined in our responses below, OFN believes that the Fund should apply certification standards consistently.

Certification Criteria

As stated above, OFN believes that the certification process is fundamentally sound and meets the needs of CDFIs and their investors, as it is currently structured and implemented. If our comments below do not address a particular question, the Fund should assume that OFN is satisfied with the Fund's current practice in evaluating that aspect of the criterion.

Primary Mission Criterion

Question (a): Should the primary mission criteria differ by organization type? If so, how?

Question (b): Protecting Against Predatory Lending

(i) Should the CDFI Fund consider the types of Financial Products offered by an entity as relevant to the primary mission criteria? Specifically, should the CDFI Fund review, as part of the certification process, evidence of affordability of an entity's Financial Products to the intended customers?

(ii) How else might the CDFI Fund ensure that CDFI Certification is not given to entities that engage in what are commonly called "predatory lending practices" or include so-called "predatory lending terms" in their lending practices?

(iii) Should the CDFI Fund require entities to provide Financial Products at a cost that is at least comparable to market rates or at some minimum level of affordability to their Target Markets in order to satisfy the primary mission criteria? If yes, how should market rates or minimum levels of affordability be determined?

In earlier comments to the Fund on the "primary mission" criteria, OFN expressed concern with a 2006 change to the regulations that eliminated the requirement that an applicant and all its affiliates be devoted to community development. We understand that portfolio companies of a community development venture capital firm, because of the structure of such investments, may disqualify a community development venture capital organization. We recommend that the Fund return to a requirement that all affiliates be devoted to community development, possibly with a specific and narrow exception for venture capital CDFIs; or require that a parent of any applicant be devoted to community development.

OFN strongly believes that the CDFI Fund should not assess the "affordability" of products and services in a CDFI's market. Pricing is only one element in the constellation of predatory practices the Fund hopes to play a part in eradicating. CDFIs set their pricing and select their products based on many different factors. In addition, generally accepted accounting principles recognize that there is no single "CDFI Market," due to the customized nature of financing that every CDFI engages in, and that each CDFI's market is unique.

We share with the Fund a concern about the harm predatory lenders have caused and continue to cause in America's communities. They are often the same communities in which we work and which the Fund's investments support. However, OFN believes that the combination of other certification criteria—particularly a community development mission, a provision of real development services, and accountability—will prevent predatory lenders from being certified by the Fund.

Under no circumstances should the Fund use product pricing or an attempt to determine "affordability" as a screen for certification.

Financing Entity Criterion

Question (a)(i) What minimum level of financing activity (i.e., number of transactions, dollar amount of transactions, years in operation, and/or financing) should the CDFI Fund consider to be acceptable to determine that an entity is a financing entity? (ii) How might this minimum level differ among organizational types?

Question (b)(i) Is three (3) months worth of financing capital a reasonable measure of an entity's ability to sustain its financing activities? Should the period of time be longer or shorter? (ii) What other measure(s) should the CDFI Fund use to determine that an entity can sustain its financing activities?

(c) The CDFI Fund's definition of Financial Products includes Loan, Equity Investments, and similar financing activities (as determined by the CDFI Fund) including the purchase of loans originated by CDFIs and the provision of loan guarantees. Should the CDFI Fund expand this definition? If so, what other products should be included?

OFN feels strongly that the current "financing entity" test does not accurately reflect the finance-driven strategy of CDFIs and allows organizations that are not financing entities to be certified. The first set of regulations the Fund issued in October 1995 called for an institution's "predominant business activity" to be the provision of loans and investments (Sec. 1805.200(3)(d) of the Interim Rule published in Vol. 60, no. 202 of the Federal Register). We object particularly to the way the Fund considers "provision of Financial Products, Development Services, and/or other similar financing" (Sec. 1805.201(b)(2)) rather than only financial products; *and* requires that these activities constitute only a plurality of an organization's activities (as outlined in the preamble to the 1999 Interim Rule making these changes, published in the Federal Register, Vol. 64, no. 210, page 59078). Instead, provision of financial products and services should constitute a majority of the CDFI's activities and financing should be an integral part of the CDFI's strategy.

In making Technical Assistance Awards, the Fund has granted awards to CDFIs in formation with the condition that the organization be certified within a defined time period. It should ensure that this practice also extends to depository CDFIs in formation.

Target Market Criterion

Question (a): Are the CDFI Fund's Target Market options (Investment Area, Low Income Target Population, and Other Target Populations) clear? If not, how can the CDFI Fund make the options more clear?

Question (b): Should a certification applicant be required to demonstrate a track record of serving the requested Target Market? If so, what is an appropriate minimum time frame to establish such a track record? Please provide reasons to support your response.

Question (c): Should the CDFI Fund allow different types of organizations to meet the Target Market requirement at different benchmarks (i.e., percentage of activities directed toward Target Market could deviate from the required 60 percent level for certain types of organizations)? If so, what level of activity would be acceptable for specific organization types?

Question (d): Should certification applicants be required to have a physical presence in their Target Market (i.e., a branch, an office, local partner)? If so, what is an acceptable minimum level of presence?

The market areas served by CDFIs vary as much as the CDFIs themselves. The Fund's own three options for Target Markets—Low-Income Area, Low income Target Populations, or Other Targeted Populations—imply that physical presence is not necessarily connected to the Target Market. For CDFIs in rural, thinly populated areas or with Target Markets that encompass a multi-state region or the entire country, a "physical presence" is simply unworkable; these CDFIs serve Targeted Populations with the location of those populations a secondary consideration. In addition, Internet-based delivery of financial services is becoming ever more common, especially for community credit unions and banks, and it is unreasonable to penalize an institution that leverages its electronic capacity to serve broader underserved markets. Again, the Fund should respect CDFIs' own assessments of the operations needed to provide service to a target market.

It is possible that the 60 percent threshold for services to a target market could appropriately vary for different types of organizations, but OFN does not believe that the Fund or the industry has sufficient data to make this determination. We suggest that the Fund act on the Community Development Bankers Association's suggestion to conduct additional research to determine whether a different standard might be applicable to bank CDFIs, and seriously consider any recommendations from other associations representing specific sectors that offer a valid case for a different level of services to the Target Market.

Accountability Criterion

Question (a)(i) How many governing and/or advisory board members representing a Target Market should the CDFI Fund require to determine that an entity is accountable to its Target Market? (ii) How should the geographic size, population density of the Target Market, and/or board type (governing versus advisory) factor into the number of representative board members necessary to demonstrate accountability to a Target Market?

Question (b): Should the CDFI Fund expand or restrict the ways that board members can be deemed to be representative of a Target Market?

Question (c)(i) Should the CDFI Fund continue to allow certification applicants to demonstrate accountability to Target Markets through "other mechanisms" (i.e. annual meetings, surveys)? (ii) If so, what additional types of mechanisms should be considered to demonstrate accountability?

In this area as well, the Fund should recognize the variety of CDFI structures and strategies. Prescribing a particular number or proportion of board members that would suit the myriad CDFI circumstances—small neighborhood credit unions, national loan funds, rural institutions drawing from a more sparsely-populated target market—would not be possible, nor would a listing of the ways in which board members might be accountable. It would go against the Fund's purpose of supporting CDFIs based on their "market-up" form and structure.

The Fund should continue to allow CDFIs to use "other mechanisms." If the Fund fears that institutions might circumvent accountability requirements with weak "other mechanisms," it could consider requiring that the information from these "other mechanisms" be used in a formal, codified way (i.e., that the CDFI's bylaws state the role of an Advisory Board).

Development Services Criterion

Question (a): What minimum level of Development Services should be expected of a CDFI (i.e., is one-on-one counseling enough or should training be more formal and standardized)?

Question (b) Should the CDFI require an entity to provide Development Services that are linked to each Financial Product that it offers?

Question (c): Should Development Services include broad efforts to increase financial education and literacy within an entity's Target Market?

As with other criteria, the Fund cannot prescribe the amount and scope of development services in a way that suits the needs of all CDFIs. Though some CDFIs offer formal development services including classroom training, many others offer one-on-one counseling that is equally as valuable. A CDFI that guides a borrower through all the steps of the loan process provides critical development services that build borrower capacity; in fact, such services are part of what distinguish CDFIs from more conventional lenders.

While most Development Services have either a direct or an indirect link to a borrower's ability to access Financial Products, the needs of each borrower are very individualized. For example, an individual may require significant credit counseling and a class on becoming a homeowner before they are ready to purchase their first home. By contrast, an experienced housing developer knows how to manage credit, but only needs a piece of gap financing to make a project feasible. We strongly discourage the CDFI Fund from requiring certification applicants to provide Development Services linked to each Financial Product it offers.

If, as the questions in the "Primary Mission" section of the request for comments suggests, the Fund is concerned with preventing the certification of predatory lenders, the suggestion that the Development Services criterion could be fulfilled by "broad efforts to increase financial education and literacy" seems more open to abuse than other criteria. A predatory lender could suggest that providing advertisements or other unspecific financial literacy information was meeting this criterion. We suggest that the Fund, at minimum, not consider these activities as the *only* Development Service offered by an applicant.

Nongovernment Entity Criterion

Question (a) What minimum levels of government support for an entity's operations (e.g. funding and capitalization) or governmental involvement in an entity's lending or investment decisions (e.g. underwriting criteria or loan approval) should be considered acceptable for certification?

Question (b): Should governmental "operations support" and government "involvement in lending and investment decisions" be considered separately or should evidence of both be required in order to deem an entity as having failed to satisfy the non-governmental entity criteria.

OFN believes strongly that CDFI certification must be restricted to private-sector entities only, and we commend the Fund for effecting strong standards on this criterion. The current standards to restrict government control of operations have been adequate.

We do recognize, however, that government funding does not necessarily lead to government control of decisions made with that funding, any more than a CDFI Fund award constitutes federal government "control" of a CDFI. Therefore, we support separate consideration of government support and of government involvement in funding and investment decisions.

Again, however, the Fund cannot compile a "one-size-fits-all" list of ways that government might participate in a CDFI's activities.

Certification Application

Question (a): Should an electronic, web-based CDFI certification application process be implemented and if so, should a paper application continue to be accepted?

Question (b)(i): Should CDFI certification status extend for a fixed period of time before it expires? If so, is three (3) years an appropriate decision?

Question (b)(ii): Should CDFI certification be continued indefinitely if the certified CDFI does not request an award from the CDFI Fund?

Question (b)(iii): Is there any policy justification to designate different certification period for different types of organizations? If so, how long should certification periods be for specific types of organizations?

Question (c): What should be the primary components of a recertification process?

While CDFIs have found the electronic application process useful, and we recommend that the Fund explore a web-based process, we urge the Fund to retain the option of paper certification applications for CDFIs in rural areas without broadband internet access, those with otherwise limited technology, or who simply find a paper application easier to compile and maintain in their records.

OFN believes that the Fund should regularly recertify CDFIs for a period of five years. Though a recertification process should consider the same criteria as an initial certification process, the application should be less comprehensive. An expanded version of the Fund's "certification of material event" form, which asks CDFIs to elaborate on changes that affect the certification criteria, may be an appropriate model for a recertification application.

In addition, CDFIs that have been rated by OFN's CDFI Assessment and Ratings System (CARS™) have undergone a rigorous analysis of their mission, financial capacity, and governance.[2] The Fund should use a current satisfactory CARS™ rating as evidence of meeting appropriate certification criteria. OFN welcomes the opportunity to discuss the elements of a CARS™ rating that are substantially similar to certification criteria.

Because "CDFI Certification" has developed a meaning outside the Fund, we believe the Fund should continue to offer certification even to those institutions that do not apply for awards. Such an institution may be a recipient of Bank Enterprise Award funds or New Markets Tax Credit allocations that require CDFI-certified status, as well as investments from private investors that impose conditions discussed earlier in this letter.

Conclusion

Opportunity Finance Network believes that the current certification process has served the industry well. We strongly urge the Fund to maintain its current process and particularly not to make changes that inappropriately assess the operations of individual CDFIs.

We welcome to opportunity to discuss our comments and the Fund's plans further. Please do not hesitate to contact me at 215.320.4304 or mpinsky@opportunityfinance.net if you have questions or concerns.

Thank you again for the opportunity to comment.

Sincerely,

Mark Pinsky

Mark Pinsky
President and CEO

[2] For more on CARS™, see "CARS™ on the Road—Edition 3," available at http://opportunityfinance.net/store/Downloads/CARS_On_The_Road_edition3.pdf