

Cascade

a community development publication of the Federal Reserve Bank of Philadelphia

New Report Spotlights Growing CDFI Strength, Effectiveness

By Allyson B. Randolph, Director of External Affairs, National Community Capital Association

CDFIs are bigger, stronger, and more innovative. So says National Community Capital's recent publication, "Charting CDFI Progress – The 1999 Report." This analysis of year-end 1998 data reveals that CDFIs are successfully leveraging billions of dollars into economically disadvantaged communities and that those dollars are making a difference.

"The data are clear. The CDFI industry is in a major growth phase—both in terms of the capital they are able to bring in and the opportunities they are able to create in poor communities," says Kathy Stearns, National Community Capital's Director of Financing & Development.

Each year, the National Community Capital Association conducts a comprehensive analysis of community development financial institutions', or CDFI, performance (Table 1). At year-end 1998 the 51 CDFIs in the sample included many of the largest, most active, and most innovative institutions in the country.¹ National Community Capital analyzes the financial and organizational performance, the financing activities, and the social impact of these CDFIs over the past year and compares those data to past years'.

"We are interested in all aspects of a CDFI's performance, and we go to great lengths to make sure the data we get are accurate and truly

represent a CDFI's work over the year," says Stearns.

Several key findings from year-end illustrate the growing strength and effectiveness of the CDFI industry.

CDFIs are managing increasingly larger amounts of capital. The 51 CDFIs saw a 56 percent increase of their loan capital under management—from \$475 million at year-end 1997 to \$742 million at year-end 1998 (Figure 1). This was the second consecutive year in which the CDFIs surveyed saw an increase in loan capital of more than 50 percent. In addition, a greater number of CDFIs surveyed saw a

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New Fair Lending Exam Procedures: How Does a Bank Prepare?

By Donald W. James

This past summer, the Federal Reserve Bank of Philadelphia presented two seminars on the new interagency fair lending examination procedures. All banks in the Third Federal Reserve District were invited to attend. While it is important for bankers to understand these procedures, it is also important for consumers to have a basic knowledge as well. After all, the purpose of the procedures is to ensure that all credit applicants are treated

equally. This article will briefly discuss the genesis of these procedures, provide an overview of them directed at nonbankers, and offer some suggestions to bankers on how to prepare for their first examination.

The fair lending examination procedures address enforcement of two federal civil rights laws: the Equal Credit Opportunity Act (ECOA) and the Fair Housing Act (FHA). Both of these laws prohibit discrimination against credit applicants because of irrelevant factors

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¹ Each year National Community Capital asks its member CDFIs to complete a survey that details their financial and organizational status as of the end of the year and their financing activity during the calendar year. National Community Capital staff verify the data and adjust them where necessary. Because National Community Capital's membership changes from year to year, staff account for changes in statistics that are clearly the result of changes in the sample.

Table 1. Key Characteristics of CDFI Sample, 1998

Characteristic	Sample Average	Sample Total
Total Capital (\$millions)	\$14.6	\$742
Net assets for lending to total capital ratio*	32%	37%
Loans outstanding (\$millions)	\$9.4	\$471
Loans outstanding (number)	199	9,939
Average loan outstanding*	\$67,784	\$47,415
Term of loans outstanding (months)	64	
Interest rate charged for loans	7.7%	
Cost of funds	2.1%	
Term of borrowed capital (months)	96	
Loan loss reserve* (as % of loans outstanding)	7.3%	4.6%
Loans >90 days past due* (as % of loans outstanding)	4.5%	2.8%
Operating revenue (\$millions)	\$2.1	\$109
Total expenses (\$millions)	\$1.7	\$ 86
Self-sufficiency ratio	76%	84%

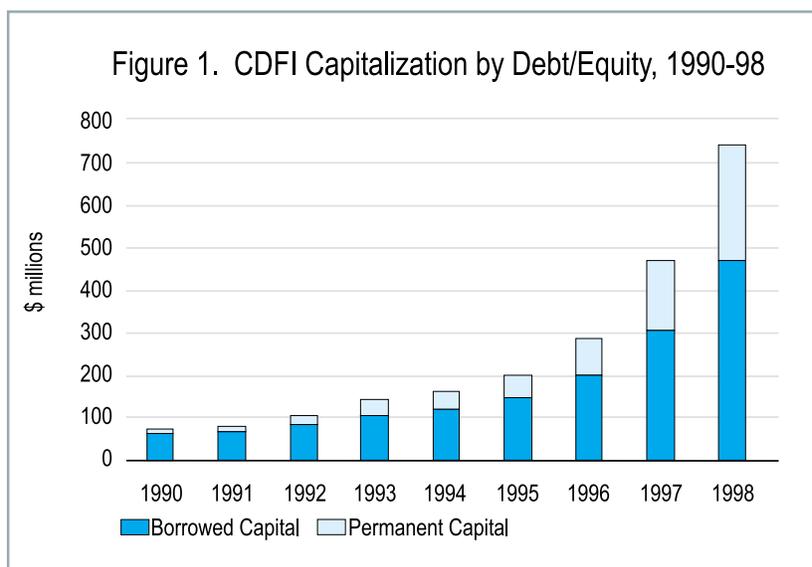
*The weighted average ratio is given for net assets for lending to total capital ratio, average loan outstanding, loan loss reserve percentage, loans past due percentage, and self-sufficiency ratio. It is the sum of the numerator divided by the sum of the denominator, which, in effect, gives greater weight to the larger organizations.

What Are CDFIs?

CDFIs are financial intermediaries that have community development as their primary mission and that develop a range of strategies to carry out that mission. CDFIs include community development loan funds, community development credit unions, microenterprise development organizations, community development venture capital funds, and community development banks. CDFIs make loans that conventional financial institutions don't, and they link their financing to development services. CDFIs provide financing to create quality affordable housing, economic opportunities, and community infrastructure in economically disadvantaged urban, rural, and reservation-based communities. More than 450 CDFIs operate in the United States today.

substantial increase in loan capital. About half of the CDFIs surveyed saw an increase in loan capital of more than 25 percent. Encouraged by the CDFI Fund's Bank Enterprise Awards (BEA) program, banks have contributed significantly to CDFIs' increased capital. Capital from conventional financial institutions constituted 20 percent of CDFIs' borrowed capital at year-end 1998—up from 17 percent just a year before (Table 2).

CDFIs are growing in capital strength as well. Net assets dedicated to lending² accounted for 37 percent of capital managed by the CDFIs in the sample at year-end 1998—a slight increase over the 36 percent figure for year-end 1997. All of the CDFIs in National Community Capital's survey are nonprofits and most are unregulated. A strong



capital base is critical to the long-term performance and permanence of these institutions. A key contributing factor to this increase was the

CDFI Fund of the U.S. Department of the Treasury. Through 1998, the CDFI Fund has awarded more than \$110 million in equity to CDFIs, of

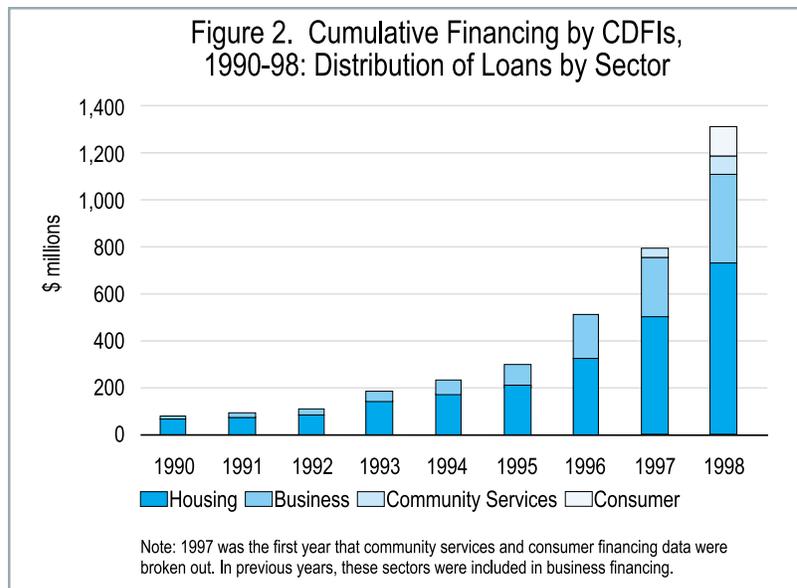
² Net assets dedicated to lending is often referred to as equity or permanent capital, and is defined as donated capital that is temporarily or permanently restricted to lending/investing, as well as retained earnings that the CDFI's board has designated for lending or investing.

Table 2. Sources of Borrowed Capital, 1990-98

Source	1990	1993	1996	1997	1998
Government	12%	10%	13%	14%	19%
Foundations (program-related investments)	20%	30%	28%	27%	25%
Conventional financial institutions	11%	19%	17%	17%	20%
Religious institutions	23%	17%	17%	16%	15%
Individuals	27%	17%	13%	11%	8%
Other	7%	7%	12%	10%	8%
Nonbank financial institutions (asked from 1997 on)				5%	5%

Data exclude credit unions in all years and Self-Help in 1997 and 1998 because their capital structures are so different from those of the other CDFIs in the sample that they significantly skew the data.

Figure 2. Cumulative Financing by CDFIs, 1990-98: Distribution of Loans by Sector



allowed CDFIs to have a positive impact on the communities and people they seek to serve. Through their financing activity, the CDFIs in the survey have helped create more than 86,000 housing units, 66,000 jobs, and 310 million square feet of nonresidential space.

“The CDFI industry has capitalized on the current boom economy and is helping distressed communities make the most of this prosperity,” says Mark Pinsky, National Community Capital’s executive director.

CDFIs are developing innovative mechanisms to reach deeper and broader in economically distressed communities. Several CDFIs, including The Reinvestment Fund (formerly DVCRF) in Philadelphia, have created venture capital arms as part of their community development strategies. By providing venture capital, CDFIs can help finance businesses that have the potential to create large numbers of jobs in distressed communities. The New Hampshire Community Loan Fund in Concord, New Hampshire, is financing a program to train former welfare

which \$38 million was awarded to CDFIs in the survey.

This new capital is reaching communities in need. Liquidity³ levels for the CDFIs in the survey remained stable at 25 percent despite the significant increase in capital under management. This figure is especially notable since most CDFIs have investor-imposed liquidity requirements of 15 percent to 20 percent.

CDFIs are successfully managing the risk of their financing. The 51 CDFIs in the survey have provided cumulative financing totaling more than \$1.3 billion while maintaining a loss rate of only 1.7 percent (Figure 2).

Finally, CDFIs are translating their increased capital size and strength into community impact. Increased capital size and strength and prudent risk management have

³ Liquidity, the amount of capital not yet loaned or committed, is defined as 1 - [(loans outstanding + committed loans)/total capital].

recipients to be in-home health care providers. Cascadia Revolving Fund in Seattle, Washington, has created a Rural Development Investment Fund (RDIF) through which Cascadia provides equity-like financing (low interest-rate debt on a long amortization schedule with a revenue-based fee) to entrepreneurs in rural Washington state.

"If this report says anything, it says that CDFIs are a strong and growing force working to benefit poor communities in this country. CDFIs are a critical strategy for addressing some of our nation's most pressing social problems," states National Community Capital's Pinsky.

Copies of "Charting CDFI

Progress" are available at a cost of \$20 by calling National Community Capital. Also available is a companion report, "CDFIs Side by Side." This report, also \$20, compares 51 CDFIs that have been divided into six "peer" groups according to financing focus and capital size. To request copies, call Kyong Hui Park at 215-923-4754 or email her at: kyongp@communitycapital.org.

What Is National Community Capital?

Established in 1986, National Community Capital Association is a national community development financial intermediary that helps institutions and individuals provide capital that increases resources and opportunities for economically disadvantaged people and communities.

National Community Capital provides financing to CDFIs on a performance basis and financial management services for CDFI investors. It also conducts training seminars and conferences, provides fee-based consulting services, and disseminates information on technical and policy issues throughout the industry.

New Fair Lending Exam Procedures: How Does a Bank Prepare?

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such as race, national origin, sex, or religion, among others. The ECOA covers all types of lending; the FHA covers only home-related lending.

Over two years ago, the Federal Financial Institutions Examination Council (FFIEC) created a task force to revise these procedures. The old procedures were not particularly effective at detecting illegal discrimination, and they were not applied uniformly by all of the regulatory agencies. The FFIEC approved the new procedures on December 4, 1998, and issued them on January 5, 1999.

The new procedures establish a uniform approach to be used by the Office of the Comptroller of the Currency, Federal Deposit Insurance Corporation, Federal Reserve System, Office of Thrift Supervision, and National Credit Union Administration. They are intended to provide a basic and flexible framework to be used for the majority of fair lending examinations, but each agency may augment them with additional procedures.

The fair lending examination procedures are divided into four main sections:

- guidelines for the scope of the examination;
- compliance management review;
- examination procedures;
- obtaining and evaluating responses from the lender.

Guidelines for Scope of Examination

Before arriving at the bank, examiners determine the breadth, or scope, of the examination, identifying which loan products are offered by the bank, the size of each portfolio, the extent and demographic composition of the lender's market area, the organization of the lender's decision-making process, and which prohibited basis (national origin, age, sex, etc.) is most likely to be found. They then use an eight-step process to evaluate the potential for discriminatory conduct.

One of the more detailed steps in the process involves identifying discrimination risk factors in residential lending. This step is important because it places more emphasis on certain elements of an institution's loan program than was seen in the past. In this step, the examiner

looks for indicators of the more obvious forms of discrimination¹ but also gives equal weight to less obvious areas.² Two other steps outline similar reviews of risk factors for consumer and commercial lending.

At the end of the "scoping process," the examiner selects the areas that warrant examination based on the relative risk levels identified during this process.

Compliance Management Review

This section of the examination is conducted in tandem with the first, since the strength of a bank's compliance management program influences the level of risk in its lending operations. The examiner determines the breadth and depth of the analysis that will be conducted based on an evaluation of the compliance management measures employed by the institution and the reliability of the institution's practices and procedures for ensuring continued fair lending compliance.

Generally, the review will focus on:

- Determining whether the policies and procedures of the institution enable management to prevent,

or to identify and self-correct, illegal disparate treatment in the transactions that relate to the products and issues identified in the first section;

- Obtaining a thorough understanding of the manner by which management addresses its fair lending responsibilities with respect to (a) the institution's lending practices and standards, (b) training and other application-processing aids, (c) guidance to employees in dealing with customers, and (d) its marketing or other promotion of products and services.

Examination Procedures

Having determined the scope of the examination, the examiner, on-site, compares the files of approved and denied applications for the loan type(s) identified in the scoping process. For example, the examiner may have decided that the most likely problem area lies in home-improvement loans and that race is the prohibited factor.

The examiner reviews the files for home-improvement loans and identifies the "best" minority applicant file (called the benchmark) that was denied and compares it with a nonminority applicant file that was approved but that was less qualified than the benchmark. Approved nonminority applicants who appear no better qualified than the benchmark applicant are identified as "overlap approvals." If there are no overlap approvals, there are no instances of disparate treatment in the comparative file review for which the lender must account. If there are overlap approvals, the examiner may ask to meet with the appropriate loan personnel, who will be asked to explain the discrepancies found. These discussions between the examiner and lenders are new. Previously, management, not the lenders who made the credit decisions, was initially asked to explain discrepancies. Under the new procedures, the

lender bears the burden of proof that no discrimination occurred.

Obtaining and Evaluating Lenders' Responses and Concluding the Examination

After completing the analyses required under the examination procedures section, including discussions with appropriate lenders about specific credit decisions, the examiner must present his or her findings to the institution's management. At this time, management will be asked to explain unresolved issues involving:

- Any overt evidence of disparate treatment on a prohibited basis;
- All instances of apparent disparate treatment (e.g., overlaps) either in the underwriting of loans or in loan prices, terms, or conditions;
- All instances of apparent disparate treatment in the form of discriminatory steering, redlining, or marketing policies or practices;
- All instances in which a denied prohibited-basis applicant was not afforded the same level of assistance or the same benefit of discretion as an approved control group applicant who was no better qualified with regard to the reason for denial;
- All instances in which a prohibited-basis applicant received conspicuously less favorable treatment by the lender than was customary from the lender or required by the lender's policy.

Unless there are legitimate, nondiscriminatory explanations for each of the "matched" files, the examiner could conclude that the lender is in violation of the applicable fair lending laws.

Conclusion

A fair lending violation can occur even in the absence of intent to



discriminate. Proving intent is not required. In fact, in most cases, lenders probably do not intend to discriminate. Often, discrimination occurs because a financial institution has unevenly applied its underwriting policy or because it has no underwriting policy at all. But, whether discrimination is intentional or not, the consequences can be expensive. Recently, the Department of Justice announced a settlement in which First American Corp. agreed to pay \$3 million in damages to black borrowers who were denied home-improvement loans because First American's subsidiary overrode judgments made by its own credit scoring system.

Lenders can use the new inter-agency procedures as a guide for performing their own internal fair lending analyses to help ensure that all applicants are treated fairly. Financial institutions are in business to make money by extending credit; certainly, making sound loans—and making them regardless of an applicant's race, religion or other characteristic—is in the best interests of all lenders' bottom line.

Note: The new procedures are available on the FFIEC web site at www.ffiec.gov/pr010599.htm.

¹ Such as overt (for example, maintaining a policy against lending to a certain race), redlining (for example, not lending in a certain geographic area), and disparate treatment in underwriting (for example, substantial disparities among approval/denial rates of protected and nonprotected classes).

² These areas include disparate treatment in pricing (for example, substantial disparities among prices being quoted or charged to applicants who differ as to their prohibited-basis characteristics); disparate treatment by steering (for example, lack of clear, objective standards for classifying applicants as "prime" or "subprime" borrowers); and disparate treatment in marketing (for example, advertising only in media serving nonminority areas of the market).

How to Prepare for a Fair Lending Examination

1. Institute a second review process so that all denials are reviewed by at least two people.
2. Evaluate your assessment area for the percentage of minority populations and identify census tracts with large minority populations. Determine if your bank's lending reflects the demographics of your assessment area. How large is the market? Are you reaching it? Are there any gaps? If so, why?
3. Check HMDA disparity ratios. Compare the minority denial rate to the nonminority denial rate and determine if minorities are more likely to be denied. If so, be prepared to explain why. Perhaps you targeted your marketing of a loan product to an area with a large minority population and had a very good response. But while you may have increased the number of loans, you may also have increased the number of denied applications. Conduct the same exercise for gender.
4. Be aware of changes in bank management, new products, and changes to existing products. Be familiar with how your products are priced. Do you use risk-based pricing, or does one size fit all?
5. Conduct your own fair lending examination. Pick a product that you suspect is most susceptible to possible disparities in lending. Randomly pull files and compare those applications by protected groups under the ECOA with those of nonprotected groups. Are you able to identify denied applicants in protected groups who are more qualified than approved applicants in nonprotected groups?
6. Check to see if your residential mortgage department allows overages. Do any of your loan areas use risk-based pricing? If so, are there disparities in pricing between protected and nonprotected groups?
7. Find out if your institution permits auto dealers who offer financing indirectly through your bank to set rates within a certain market cap. If so, you should look into that process and determine if the cap is being exceeded and who is paying the higher price: Women? Minorities? The elderly? Who benefits from the higher rate: Dealer? Bank? Both?
8. If your institution uses credit scoring, review the override practices and how they affect protected groups. Did a certain class of applicant receive overrides? Make sure the models are validated periodically.
9. Determine how loan officers are compensated. Does the incentive program discourage loan officers from working on loans of smaller amounts? Is compensation tied to loan pricing?
10. Does your bank have a minimum loan amount? A minimum income requirement? Does a minimum requirement prevent certain groups from obtaining loans?
11. Periodically review marketing programs to ensure that you are reaching all markets and document it.
12. Determine if all applicants are given the same opportunity to explain derogatory or questionable credit information. Are discounts on application fees given to certain applicants but not others?

Many financial institutions are looking for investment opportunities that meet the definition of community development under the Community Reinvestment Act, and a number of nationally known organizations have developed securities in response to this need. At a District-wide conference hosted by the Federal Reserve Bank of Philadelphia's Community and Consumer Affairs Department on December 14 near Harrisburg, Pennsylvania, bankers had an opportunity to hear from and meet with representatives of these organizations.

The conference featured organizations that have investment vehicles collateralized by single-family, multifamily, business, or commercial loans (or a combination of these). The sponsoring entities include nonprofits or for-profits and are national, statewide, or regional in scope. Some can tailor their products to a bank's marketplace and are interested in purchasing loans from banks.

Single-Family Investments

Organizations with single-family investments included Countrywide Securities Corporation, Fannie Mae, Freddie Mac, and Neighborhood Housing Services of America, Oakland, California.

Countrywide Securities is an affiliate of Countrywide Home Loans, Inc., one of the largest residential mortgage originators in the nation. A direct lender, Countrywide has 570 loan offices around the country, many in urban communities. The company will provide investors with loans or securities collateralized by loans that meet any specification, including geographic, borrower income, or loan type (government, conventional, and so forth).

Fannie Mae and Freddie Mac are the two largest secondary markets for residential loans nationally. As government-sponsored enterprises, they have made a commitment to HUD to increase the supply of mortgage money for low- and moderate-income (LMI) borrowers

and communities. They sell securities collateralized either by single-family houses in LMI communities or single-family houses sold to LMI borrowers. Both Fannie Mae and Freddie Mac will also buy loans with these characteristics from direct lenders.

Neighborhood Housing Services of America (NHSA) operates a secondary market for nonprofit lenders affiliated with the Neighborhood Reinvestment Corporation and the NeighborWorks™ network. There are NeighborWorks™ organizations in nine Third District communities: Trenton, Camden, and Vineland, New Jersey; Philadelphia, Allentown, Scranton, Lemoyne and Reading, Pennsylvania; and Wilmington, Delaware. NHSA has been buying single-family mortgages from NeighborWorks™ organizations for more than 20 years. Recently, NHSA sold its first "rated" issues, secured by loans on single-family properties in LMI communities.

Multifamily Investments

The Local Initiatives Support Corporation has established a new affiliate to respond to multifamily housing needs. The new entity, Community Development Trust, Inc., is a hybrid real estate investment trust (REIT) created to acquire multifamily properties that may be lost to the nation's affordable housing supply because of expiring Section 8 contracts. In many communities, a large amount of affordable housing was built in the late 1970s and 1980s when project-based Section 8 certificates from HUD were common.

As the Section 8 program winds down, and unit-income restrictions expire, owners are left with the difficult decision of how to keep the units affordable and not incur great tax expense in doing so. The CDT REIT is an option. CDT is acquiring its first projects with initial investments made by banks, insurance companies, and The Reinvestment Fund.

Community Lenders CDC is a newly created consortium of several small community banks based in suburban Philadelphia. It was formed to compete with larger financial institutions that actively seek multifamily loans, particularly those with low-income tax credit allocations. It will originate other types of community development loans as needed. Its particular areas of interest are Montgomery County and upper and central Bucks County.

Business and Commercial Real Estate

The Community Reinvestment Fund, Minneapolis, Minnesota, is a nonprofit secondary market for a wide range of community development loans. It has been buying loans for 10 years. Many of its loans were originated by government economic development programs, such as those of the New Jersey Redevelopment Authority. The fund sells bonds backed by commercial, business, and housing loans around the country.

Urban America, L.P., New York, New York, is a new venture created to provide urban nonresidential properties with the same types of equity and debt found in suburban markets. It has arranged \$40 million in initial funding from large financial institutions. It is actively seeking urban, commercial, office, retail, and industrial real estate properties on the East Coast. The partnership expects to create a REIT for these properties.

Community Development Financial Institutions (CDFIs)

The National Community Capital Association (NCCA), a Philadelphia-based intermediary of CDFIs, offers another opportunity for investment. It provides capital, training, and technical services to CDFIs around the country. The Third District is home to several of them. NCCA was instrumental in creating

County Housing Trust Funds: A Source for Affordable Housing Finance in Pennsylvania

By Daniel Hoffman, Policy Director, Pennsylvania Low Income Housing Coalition

Finding the financial resources needed to support affordable housing activities is always a problem. But in Pennsylvania, county governments, housing and redevelopment authorities, and non- and for-profit developers are increasingly turning to the Optional County Affordable Housing Funds Act, or Act 137 (1992), as a source of capital for a variety of affordable housing activities. Authorized by the General Assembly in 1992, Act 137 permits counties to double their recording fees and use the extra revenue (generally about \$13 per transaction) to fund affordable housing programs.

Thirty-eight of Pennsylvania's 67 counties (Table 1) have now adopted Act 137 (by statute, Philadelphia County is barred from adopting Act 137). Together, these funds raise more than \$8 million annually, according to a 1998 report published by the Pennsylvania Low Income Housing Coalition (PALIHC).

As with the more familiar state housing trust funds (Pennsylvania is among a minority of states that do not have a state housing trust fund), the Act 137 program can be described as a trust fund program because revenues raised are dedicated to affordable housing purposes. Also, the fund is nonlapsing, which means that local advocates and providers do not have to lobby each year for a specific housing appropriation. Rather, whatever sum accu-

mulates in the trust fund account is available to support housing activities.

Act 137 was written to give counties maximum flexibility re-

cracy to administer this money.

Although funds are collected by the county recorder, county housing authorities and redevelopment authorities tend to be the administra-

Table 1

Counties That Have Adopted Act 137

Adams	Columbia	Lawrence	Somerset
Allegheny	Crawford	Lebanon	Union
Armstrong	Cumberland	Lehigh	Venango
Beaver	Dauphin	Mifflin	Warren
Berks	Delaware	Monroe	Washington
Bucks	Elk	Montgomery	Westmoreland
Butler	Fayette	Northampton	Wyoming
Cambria	Indiana	Northumberland	York
Centre	Lackawanna	Pike	
Chester	Lancaster	Schuylkill	

garding how these locally raised revenues are spent. The law essentially permits any affordable housing activity to be supported by the fund, provided the activity serves a population having an income of not greater than 100 percent of the area median income. However, responses to PALIHC's 1998 survey of trust fund administrators indicate that most funds serve populations with significantly lower incomes. This is because in 32 of 38 counties, funds are used in conjunction with HOME funds. The HOME program limits participants' incomes to 80 percent of area median. The linkage to the HOME program has enabled counties to creatively use Act 137 funds without establishing a new bureau-

tors of Act 137 funds. Frequently, county planning departments or county offices of housing and community development are the administrators. Some counties have asked their own government-operated community action agencies or a countywide nonprofit agency (including 501(c)(3) community action agencies) to administer their housing trust fund programs.

Revenues Generated

Although in aggregate more than \$8 million is generated annually by Act 137, the money accrues unevenly throughout the state. The suburban Philadelphia counties, which have larger populations and more active real estate markets, as

Table 2

How Counties Spend Their Act 137 Revenues

- 27 counties fund owner-occupied moderate rehabilitation programs.
- 18 counties have down payment and/or closing cost assistance programs for first-time home buyers.
- 12 counties have used funds to develop rental housing for the elderly.
- 10 counties have developed new or substantially rehabilitated owner-occupied single-family housing.
- 9 counties support home-ownership counseling programs.
- 7 counties have funded rental assistance programs; generally these programs are for targeted purposes and provide assistance for less than three years.
- 7 counties have established housing programs for the disabled.
- 7 counties support programs benefiting the homeless.
- 2 counties are supporting fair housing programs.

well as Allegheny County have trust funds that yield revenues ranging from about \$500,000 to more than \$1 million annually. These sums are relatively significant, particularly when one realizes that the Pennsylvania Department of Community and Economic Development provided little more than \$1 million in general revenue funding for housing purposes for the entire state, excluding Philadelphia and Pittsburgh, last year. However, in some of the state's more rural counties, there are fewer real estate transactions, and thus, Act 137 raises very little money.

In creating a housing trust fund, counties such as Elk, Lawrence, and Venango, and others have tried to internally address their local housing problems. However, funds in some rural counties yield very limited revenues, often less than \$50,000 annually. That's not enough to make a significant dent in the housing problems confronting these counties, even though they have relatively small populations. Thus, though the glass is more full in these 38 counties because of Act 137, a county trust fund is not a substitute for a state housing trust fund, particularly a well-capitalized and organized one that complements and is coordinated with county efforts.

How Pennsylvania Counties Spend Their Trust Fund Dollars

Because Act 137 is flexible regarding the use of trust fund dollars, counties can spend their money in a variety of ways, and many have. Table 2 indicates some of the ways in which counties have used Act 137 revenues.

Home-ownership programming is the most frequently cited use of county trust fund revenues, but many counties support multiple activities serving owners and renters. While it is true that the larger counties tend to offer more varied programming, some of the more rural counties also use Act 137 to support multiple programs.

The PALIHC survey was very conservative in its approach to measuring the amount of production resulting from county trust funds. Table 3 reports PALIHC's estimate of affordable housing production aided by Act 137.

Distributing Funding

How does one apply for this money? Distribution of funds varies by county. In some counties, the commissioners have established very specific program priorities. In a few counties, revenues are dedicated to supporting specific activities, projects, or agencies, including local housing authorities and non-

profit organizations.

However, in other counties the use of funds is left to the discretion of the administrative entity or a special citizen advisory board created to aid in setting Act 137 priorities.

Counties in which funds have not been dedicated to specific activities tend to expend Act 137 revenues in one of two ways. In some counties, the administrative entity directly operates a program to which end-users of the funding apply for assistance. Often, these programs are making home repair loans or providing down payment assistance. However, some counties conduct a regular "request for proposal process" in which project sponsors are invited to propose uses for the trust fund revenues. PALIHC's 1998 survey of fund administrators indicates that counties change their process of distributing funds from time to time, alternating between internally driven fund distribution systems and seeking proposals from the broader community.

Ultimately, the only way to determine how a county you're interested in distributes funds is to call the county in question.

Opportunities to Participate

For lenders and developers,

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Before (left) and after (right) shots of a house in Cambria County, Pennsylvania, that was rehabilitated using money, in part, from the Cambria County Affordable Housing Trust Fund. The Cambria County Redevelopment Authority administers a housing rehabilitation program for low- and moderate-income home owners and families with special needs living in several targeted LMI communities within the county. Using funds from the Community Development Block Grant program, the Home Partnership Initiatives program, and the Cambria County Affordable Housing Trust Fund, qualified home owners receive up to \$15,000 in grant assistance for repairs to bring their properties into compliance with local housing quality standards. Approximately 30 housing rehabilitations are realized annually by the Redevelopment Authority. (Photos courtesy of Cambria County Redevelopment Authority)

EQ², Equity Equivalent, a means of providing equity to a nonprofit that meets the Office of the Comptroller of the Currency's criteria for the CRA investment test.

The Pennsylvania Community Development Bank, a program of the Pennsylvania Department of Community and Economic Development, is a new investment opportunity. It provides loans and capacity-building grants to CDFIs and other nonprofit organizations planning to meet credit needs not typically served by banks.

The Reinvestment Fund, a Philadelphia-based regional CDFI with \$60 million in assets, discussed its

operations and the investment opportunities in two affiliated corporations: the Collaborative Lending Initiative and DVCRF Ventures.

For information, contact: Diane Koehler of the Community Lenders CDC at (215) 721-2452; Judd Levy of the Community Development Trust, Inc. at (212) 271-5080; Frank Altman of the Community Reinvestment Fund at (612) 338-3050; Steve Boginsky of Countrywide Securities Corporation at 1-818-225-4969; Patricia Ednie Parsons of Fannie Mae at (781) 837-7228; Andrew Kelman of Freddie Mac at (703) 903-3932; Allyson Randolph of the National Community Capital Association at (215) 923-4754; Jack Gilbert

of Neighborhood Housing Services of America at (721) 669-5246; Joan Brodhead of the Pennsylvania Community Development Bank at (717) 783-1109; Jeremy Nowak of The Reinvestment Fund at (215) 925-1130; and Richmond McCoy of Urban America, L.P. at (212) 785-5202.

Government, Lenders, Nonprofits Tackle Multifamily Housing Issues in New Jersey *By Keith Rolland*

Rental housing became more expensive and scarce in the 1990s. In New Jersey, several initiatives are responding to a critical need for affordable rental housing for low- and moderate-income people.

A recent report from the U.S. Department of Housing and Urban Development (HUD) said that, nationwide, the number of units affordable to households at or below 30 percent of area median income dropped 5 percent from 1991 to 1997. Rents increased at twice the rate of general inflation in 1997 and 1998. For every 100 households at or below 30 percent of median income in 1997, only 36 units were both affordable and available for rent—a sharp reduction from previous years.

Another study, by the National Low Income Housing Coalition, found that New Jersey ranked second nationally in the gap between income from minimum-wage employment and the rent required for an apartment.

A multi-sector New Jersey Mul-

tifamily Housing Preservation Committee was formed in 1998 to address the long-term viability of small and medium-size rental buildings, primarily in urban centers, operated by small entrepreneurs. The committee included representatives from government agencies, banks, nonprofit developers, the Federal Reserve Banks of New York and Philadelphia, and other organizations.

A report issued by the committee in June 1999 said that owners found it difficult to refinance and upgrade their properties because of issues involving cash flow, lending, and government policies. Cash flows are restricted by low rents, high maintenance due to old housing stock with obsolete systems, high taxes, and rent controls, all of which result in thin operating margins. According to the report, banks' lending policies favor large loans and projects because of high transaction costs and the lack of a secondary market for smaller loans. Government housing subsidies of-

ten target home ownership and new or substantially renovated units. The report noted that the moderate rehabilitation required to stabilize small and medium-size rental buildings can be completed at a fraction of the cost of new construction or gut rehabilitation.

A final report issued by the Federal Reserve Banks of New York and Philadelphia this fall summarizes the recommendations of three focus groups that met this summer. The five most important solutions envisioned by the groups are:

- A new dedicated subsidy source without income restrictions;
 - A modified version of the Federal Housing Administration's Small Projects program that includes reduced third-party expenses, shorter processing time, and dedicated staffing;
 - A more favorable tax policy as incentive for improvements;
 - A mortgage insurance program for small multifamily properties;
 - Long-term self-amortizing debt.
- Two other solutions tied for a distant

sixth place: the acceptance of lead-safe as a standard when lead-free is not feasible and inclusion of commercial income in operating pro formas.

In considering options for the most pressing issue—subsidy or equity dollars—the Fed report explores two financing strategies: low-interest rehabilitation loans funded with blended public and private dollars; and an equity pool that relies solely on private investment. The pool would be managed by an intermediary, which would also provide technical assistance to owners.

Meanwhile, the New Jersey Department of Community Affairs (NJDCA) has committed \$7.5 million in low-interest loans for a Downtown Living program to help stimulate development of new market-rate rental housing primarily in urban areas. Priority is being given to projects that demonstrate how a market rate rental project can be integrated with other development, such as retail or office projects or home ownership. Priority geographic areas in the Third Federal Reserve District include Camden, Trenton, Pleasantville, and Vineland, N.J. Bank financing is expected to complement an NJDCA loan at 1 percent with a term of up to 15 years for use as a capital cost write-down or operating subsidy. A first round of applications will be decided late in 1999; a second round of applications to be announced next spring will be due in September 2000.

NJDCA was also the only state agency selected by HUD to participate in a new program that emphasizes comprehensive tenant education. The Regional Opportunity Counseling program wants to expand landlord participation in the Section 8 program and increase housing options and diversity of neighborhoods for families assisted by Section 8. According to NJDCA, approximately 70 landlords who had never participated in the Section 8 program agreed to join after learning about the tenant-education program. Furthermore, a grant from the state's HOME program has provided assistance with security deposits to families who relocated to

better housing. (For a more complete story on NJDCA's Regional Opportunity Counseling program, see page 12.)

In the fall of 1999, another state agency, The New Jersey Housing and Mortgage Finance Agency (NJHMFA), increased funding for its Multifamily Rental Housing Pro-



Chalet Gardens, Pine Hill, Camden County. This 484-unit garden apartment complex needed \$10.6 million to refinance moderate rehabilitation, including roofs, sidewalks, and brick work. The 30-year loan carries a fixed rate of 7.99 percent. (Photo courtesy of The Community Preservation Corporation)

duction Fund program from \$15 million to \$40 million. The program is intended to provide developers with a source of construction or take-out financing when bond financing is not readily available.

In another initiative, the Community Preservation Corporation (CPC), which has financed the rehabilitation and construction of more than 63,000 low- and moderate-income housing units in New York state, has raised \$60 million in five-year commitments from 16 banks to address multifamily housing needs in New Jersey. Justin Peyser, CPC New Jersey Director, said that

CPC's goals in New Jersey are to provide renovation financing where needed, to stimulate the development of a renovation industry in the Garden State, and to give owners of both occupied and vacant buildings the know-how to put together rental rehabilitation financing packages. CPC plans to concentrate on northern New Jersey but will consider deals in the southern part of the state, Peyser said.

CPC New Jersey has closed five loans totaling \$48,430,000 for moderate rehabilitation of 2,546 units since it opened an office in Jersey City, N.J. in December 1998. The five financing packages have focused primarily on the purchase of distressed, occupied apartment buildings built before World War II that needed moderate rehabilitation. The financing packages have not involved subsidies. The five include a \$10.6 million refinancing for Chalet Gardens, a 484-unit garden apartment complex in Pine Hill, Camden County, N.J. In addition, CPC has committed financing for two buildings in Hudson and Union counties involving the conversion of a 14-unit vacant building to eight apartments and of a commercial building to 12 units and two stores.

For information, contact: New Jersey Multifamily Housing Preservation Committee members Robert Riggs, Federal Reserve Bank of New York, at (212) 720-5912 or Dede Myers, Federal Reserve Bank of Philadelphia, at (215) 574-6482; Richard Montemore, NJDCA Downtown Living Program, at (609) 633-6302; Roy Ziegler, NJDCA Regional Opportunity Counseling Program, at (609) 633-8105; Karen Torian, NJHMFA Multifamily Rental Housing Production Fund Program, at (609) 278-7518; and Justin Peyser, CPC New Jersey, at (201) 547-5626.

NJDCA Launches Programs That Provide Tenant Education and Security-Deposit Assistance

By Roy Ziegler, New Jersey Department of Community Affairs, Division of Housing and Community Resources

The New Jersey Department of Community Affairs (NJDCA) was the only state agency selected by HUD to participate in the Regional Opportunity Counseling (ROC) program. Fifteen cities, including Philadelphia and Baltimore, have also been selected. ROC's goal is to expand landlords' participation in the Section 8 housing program and increase housing options and diversity of neighborhoods for Section 8-assisted families.

Preliminary data collection and staffing began in 1998, and the program began selecting families in early 1999.

New Jersey's program is unique in that it places strong emphasis on tenant education. Working in conjunction with the University of Medicine and Dentistry, the department developed a comprehensive tenant-education package, which includes video instruction and classroom participation to teach families effective house-cleaning techniques for creating a healthier and safer home environment. Coloring books have been produced to teach children good housekeeping skills, and workbooks are provided to the parents. Families who relocate with program assistance are monitored quarterly to assess the conditions of their housing. Participants who maintain neat, clean, and healthy

home environments and who abide by their lease requirements are awarded certificates of achievement each year.

Landlords have praised the Regional Opportunity Counseling program for its innovative approach with tenants and for promoting both healthier and safer housing and landlord/tenant cooperation. Fifty-nine landlords who had never participated in the Section 8 program have agreed to join after learning about the tenant-education program. This will vastly expand families' available housing choices.

A grant from the state's HOME program was awarded to the ROC program to provide security-deposit assistance to families who wish to relocate to better housing. The cost of a security deposit, which averages about \$1200, had been a critical barrier to mobility. In 1999, 30 families received security-deposit assistance.

Also in 1999, some 50 families relocated to better quality neighborhoods in the Newark and Jersey City metropolitan areas. The tenant-education course had prepared these families for living in better housing and better neighborhoods. The addition of approximately 70 new participating landlords provided a greater selection of housing and locations for the families.

However, NJDCA has learned one thing from the first year of this program: tenant education must continually be reinforced for most of the families. Specifically, two issues must be addressed: (1) the problems associated with making the transition from a generation or two of living in housing that is marginally maintained to living in housing of better quality and (2) tenants' response of not caring for the property as would normally be expected.

Happily, reinforcing tenant education is beginning to make a real difference. Some families have moved a second time to even better neighborhoods more remote from the central city area.

For about two-thirds of these families, the security-deposit grant was the critical factor in obtaining their apartments.

The Regional Opportunity Counseling program also provides housing counseling and fair housing advocacy for tenants and home repair workshops for landlords.

For more information about the ROC program, call Roy Ziegler at the Division of Housing and Community Resources at 609-633-8105.

Business Access to Capital and Credit Conference: Summary of Proceedings Available

The Community Affairs Department of the Federal Reserve Bank of Philadelphia has published a summary of the proceedings of the conference on Business Access to Capital and Credit. The conference, which was held in March 1999, brought together distinguished economists and scholars from around the country who presented papers on topics such as credit for minority-owned businesses, bank consolidation and the small-business lending relationship, credit scoring, and microenterprise lending. Copies of the summary are available, but supplies are limited. If you'd like a copy, call Betty Carol Floyd at 215-574-6458 or email a request to her at betty.c.floyd@phil.frb.org.

Interested readers can access the complete proceedings or a summary at the Chicago Fed's CEDRIC web site: <http://www.frbchi.org/cedric/cedric.html>.

Community Affairs Has Expanded Its Presence on Web Site

Do you have a question about community development or CRA? Do you need to know what types of resources are available for small businesses in Pennsylvania, New Jersey, and Delaware? Do you need information about Federal Reserve regulations?

Help with these questions, and many others, is now just a click away. Visit the Philadelphia Fed's newly designed web site at www.phil.frb.org and click on the Community Affairs button. That's all you have to do to find a wealth of material related to community and economic development.

The Community Affairs Department's portion of the Bank's web site has been greatly expanded. Now you can link to many of the department's publications, including the latest issue of *Cascade*. You'll also have access to the lender's profiles, which highlight demographic data and lending patterns for residential mortgages and small-business loans. The profiles also identify housing and economic development programs and partners in various communities in the Third Federal Reserve District. And the electronic versions of the profiles will be updated annually, making them an even more valuable resource.

The Community Affairs pages will also take you to related links outside the Philadelphia Fed. For example, you can find out about the Partners software from the Atlanta Fed; you can tap the new CEDRIC (Consumer and Economic Development Research and Information Center) site at the Chicago Fed; or you can visit HUD's site to find out about empowerment zones and enterprise communities.

Our web address—www.phil.frb.org—hasn't changed. But the information you'll find there has!



Electronic Transfer Accounts Benefit Both Financial Institutions and Consumers

To enhance its electronic payments program, the U.S. Treasury has created a new option for those who receive federal payments: electronic transfer accounts (ETAs). Millions of recipients of federal benefit, wage, salary, and retirement funds can now receive their money electronically rather than by check, even if they don't have a traditional bank account.

This easy-to-use, low-cost way of receiving funds benefits consumers because it's secure and easily accessible and it makes record-keeping simple. Financial institutions can also benefit from offering these special accounts because ETAs allow them to expand their customer base, receive credit under the CRA service test, and provide services to those outside the financial mainstream.

A New Product for New Customers

As required by the Debt Collection Act of 1996, most federal payments, except tax refunds, must now be made via electronic funds transfer. In response, the Treasury designed ETAs for federally insured banks, savings and loans, and credit unions. To become ETA providers, financial institutions must sign a Financial Agency Agreement with the Treasury.

The ETA program allows financial institutions to increase a community's access to financial services and mold the ETAs to their community's unique needs, such as accepting deposits other than federal payments and offering interest-bearing or noninterest-bearing accounts. They can close accounts for misuse or fraud.

Banks, savings and loans, and

credit unions will receive a one-time set-up fee for each new ETA.

To support financial institutions, the Treasury is providing free in-bank materials for consumers and conducting a nationwide marketing campaign to get qualified people to open ETAs. Financial institutions can call 1-888-382-3725 to find out more about the program or request an ETA enrollment kit.

Demographically, the majority of federal check recipients are concentrated in urban areas. And more than half of all federal payments go to 10 states; this top 10 includes New Jersey and Pennsylvania.

A Safe, Simple Method for Electronic Deposits

Through the ETA program, recipients of federal payments can enjoy the safe, simple, and secure ben-

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Act 137 offers opportunities to participate. The PALIHC survey indicates that aside from federal resources, the home-ownership programs administered by county funds are not extensively leveraged. Proposals that bring “housing smarts” and additional public and private capital to the fore are likely to be welcomed by trust fund administrators. Lenders should seek to link CRA mortgages and home re-

pair loan products or Federal Home Loan Bank closing cost assistance to Act 137 programs. Similarly, although the Pennsylvania Housing Finance Agency does not specifically reward developers who use county trust funds, Act 137 can provide an effective way of closing finance gaps or lowering rent rates associated with projects developed with tax credits and/or tax-exempt bonds.

Counties have used their limit-

ed trust fund dollars in a variety of ways, often quite creatively, but more opportunities to leverage this flexible resource exist. With a more invigorated state housing policy providing additional resources to trust-fund-backed activities and an engaged community of lenders and for- and nonprofit developers working with county trust funds, Pennsylvania can make even better use of the valuable tool that Act 137 is.

Table 3
Units Assisted by Act 137 Funds

- 221 new owner-occupied units constructed
- 1,535 owner-occupied units rehabilitated
- 1,315 rental units developed or rehabilitated, including 582 units for the elderly
- 2,084 home buyers provided with closing cost and/or down payment assistance
- 84 disabled individuals (mostly MH/MR) provided with group-home housing

In Memoriam: Frederick M. Manning

Fred Manning, former Vice President and Community Affairs Officer at the Philadelphia Fed, died on September 17, 1999. Fred had taken disability leave in August 1998 because of a chronic, long-term illness, thus ending a distinguished career with the Philadelphia Reserve Bank that spanned 35 years.

Fred had directed community development efforts at the Philadelphia Fed from 1981 through early 1998 and was a leader in the System when he established a separate Community and Consumer Affairs Department in 1984. During his career, Fred was a frequent speaker about community development and the Community Reinvestment Act, not only within the region but also nationally and even internationally. Fred’s own community activities covered service as a director of the Philadelphia Development Partnership and as an advisor to the Delaware Valley Mortgage Plan and the Philadelphia chapters of Neighborhood Housing Services and Habitat for Humanity.

Prior to his becoming head of the Community and Consumer Affairs function, Fred served in several other positions within the Philadelphia Fed, including management responsibilities as chief examining officer in the bank supervision area, as personnel officer, and as a loaned executive to the Board of Governors in Washington, D.C.

Fred’s approach to community development was always straightforward and mirrored his outlook on life in general. In his words: “Simple logic tells us that we need each other.” Fred will be missed.

Written by Richard W. Lang, Senior Vice President and Director of Research, Federal Reserve Bank of Philadelphia

Electronic Transfer Accounts Benefit Both Financial Institutions and Consumers

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efits of having their payments deposited electronically directly into their accounts. Potential customers who open ETAs can gain access to financial services at a reasonable cost and benefit from the same consumer protections afforded other account holders at the same institution.

ETAs require no minimum balance, unless required by state or

federal law; allow for cash withdrawals and point-of-sale access (if available); and provide account holders with monthly statements. There is a monthly maintenance fee of \$3.

People who want ETAs for their federal payments should contact an ETA provider to sign up. By calling 1-888-382-3311 toll free, they can reach a voice response system that

will allow them to locate a list of participating financial institutions by entering a five-digit ZIP code. An Internet site, www.eta-find.gov, allows consumers to search for providers by ZIP code, city and state, metropolitan area, or name of financial institution.

This article was prepared by the Federal Reserve Bank of Dallas.



Calendar of events

Calendar of Events

Coalition of Community Development Financial Institutions (CDFI Coalition)/National CDFI Institute CDFI Partners: Capital Strategies for Building Healthy Communities

Washington, D.C.

January 27-29, 2000

For information, call Laura Schwingel at 215-923-5363. Or send email to: Lauras@cdfi.org. Also, check the web site: <http://www.cdfi.org>.

Economic Development Summit

Renaissance Hotel, Washington, D.C.

February 13-15, 2000

For information, please call 202-223-4735, or send email to: mail@urbandedevelopment.com. Or visit the web site of the Council for Urban Economic Development: www.cued.org.

United States Association for Small Business and Entrepreneurship (USASBE)/Small Business Institute Directors' Association (SBIDA) First Joint National Conference

San Antonio, Texas

February 16-20, 2000

For information, visit the following web site: www.sbaer.uca.edu/Docs/bulletins/jtconusasbesbida.htm.

Conference on Consumer Regulation in Housing Finance

Federal Reserve Bank of Cleveland

May 19, 2000

For information, call Stanley D. Longhofer, 216-579-3062 or send email to stan.longhofer@clev.frb.org.

National Community Capital Annual Training Conference

Philadelphia, November 1-4, 2000

For information, call Adina Abramowitz at 215-923-4754, ext. 205.

Cascade is published three times yearly by the Community Affairs Department of the Federal Reserve Bank of Philadelphia.

Editor _____ Sally Burke

Designer _____ Melissa Kinney

CASCADE

Federal Reserve Bank of Philadelphia
100 N. 6th Street
Philadelphia, PA 19106-1574

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