



May 6, 2016

Annie Donovan
Director, CDFI Fund
Department of the Treasury
1500 Pennsylvania Avenue, NW
Washington, DC 20220

RE: Regulatory Information Number 1559-AA00

Dear Director Donovan,

The Local Initiatives Support Corporation (LISC) is pleased to provide comments on the interim regulations implementing the Capital Magnet Fund (CMF) program.

Established in 1979, LISC is a national non-profit CDFI that is dedicated to helping community residents transform distressed neighborhoods into healthy and sustainable communities of choice and opportunity. LISC mobilizes corporate, government and philanthropic support to provide local community development organizations with loans, grants and equity investments; as well as technical and management assistance.

LISC has a nationwide footprint, with local offices in 31 cities and partnerships with 72 different organizations serving rural communities throughout the country. LISC invests approximately \$1 billion each year in these communities. Our work covers a wide range of activities, including housing, economic development, building family wealth and incomes, education, and creating healthy communities. LISC has been a recipient of several CDFI Financial Assistance awards totaling over \$30 million; has received over \$900 million in New Markets Tax Credit allocation awards; has received a \$50 million CDFI Bond Guarantee Program allocation; and in 2010, received a \$5 million CMF grant in the inaugural round of the program.

We applaud the CDFI Fund's efforts in ramping up its implementation of the CMF program and are generally pleased with the regulations and the application materials. We offer below several comments relating to the CMF interim regulations, some of which are also pertinent to the CMF application materials, the assistance agreement, and the CDFI Fund's compliance protocols.

COMMENTS ON REGULATIONS

Section 1807.104. Definitions.

Affordable Housing Fund. As currently defined, this term seems to suggest that such a fund must “revolve” the proceeds into additional affordable housing projects. It is not clear why the CDFI Fund is including the concept of a revolving loan, grant or equity investment into this particular definition when there is a stand-alone definition of a Revolving Loan Fund. While some awardees may choose to revolve the proceeds of such a fund, those that are offering longer term products that extend beyond the five year investment period and/or don’t otherwise need to revolve the funds in order to meet other programmatic requirements (e.g., leveraging requirements, program income requirements) should not be required to revolve the dollars beyond their original uses. *We therefore recommend removing the word “revolving” from this definition.*

Concerted Strategy. We are concerned that this definition is limiting, in that it requires a “formal planning document” or some other document “adopted or approved by the jurisdiction”. A concerted strategy need not be more than a strategy developed by a local community organization or CDFI to govern its investment strategies. The CDFI Fund should not put itself in a position of having to determine whether something constitutes a “formal” planning document, nor should the CDFI Fund have to require approval from a public jurisdiction. LISC, for example, as part of its Building Sustainable Communities strategy, engages at the local neighborhood level to help bring together neighborhood partners to help develop comprehensive “quality of life” plans for their neighborhood. While in most if not all cases local public officials are involved in this planning, they don’t necessarily have a formal approval role. *We therefore recommend removing from this definition the phrases “formal planning” and “adopted or approved by the jurisdiction”.*

Economic Development Activity. The definition limits economic development activities to investments in “physical structures”. *The CDFI Fund should consider expanding this definition to also include working capital loans and equipment loans to small businesses, as this is also a legitimate economic development activity.*

Preservation. The definition limits preservation activities to those that involve “refinancing”. We are concerned that the use of the term refinancing would limit these activities to projects where existing debt is being replaced by new debt. This is not the case in many preservation deals, most notably “year 15” LIHTC transactions, in which ownership of the property is being transferred to a third party, with debt replacing project equity. *We would recommend replacing the word “refinancing” with “recapitalizing.” In addition, we could also recommend adding the word “local” to “State or Federal affordable housing programs”, to fully capture all possible preservation initiatives.*

Section 1807.102. Relationship to other CDFI Fund Programs. This section states that the CDFI Fund will, in its NOFAs, outline restrictions with respect to using CMF award dollars in conjunction with other forms of assistance from the CDFI Fund. We are beginning to see as a growing trend enhanced efforts by the CDFI fund to ensure that none of its award or tax allocation dollars are mingled at the project level. We’re not sure what is driving these efforts,

because it is well understood to most in the community development field that projects often require deep subsidies from multiple sources of financing, including multiple federal sources. Furthermore, it's not clear how CDFIs are expected to track this information with respect to CDFI FA awards, since those are institution level investments that are not tied to individual projects. And with respect to NMTCs, those are not deemed to be federal financial assistance and the end beneficiary is not the CDFI, but the investor claiming the credit. *We would therefore encourage the CDFI Fund to think more deliberatively and maybe invite further public comment on issues pertaining to how its award dollars can be deployed together to support critical community and economic development needs.*

Section 1807.105. Waiver Authority. There appears to be a scrivener's error. *The third sentence should read: "For a waiver to be granted in an individual case, the CDFI Fund must determine that a waiver of the requirement would not adversely affect the achievement of the purposes of the Act. (emphasis added)"*

Section 1807.300. Eligible Purposes. 1807.300(b)(3), which delineates the tracking requirements with respect to Economic Development Activities done In Conjunction With Affordable Housing Activity, is somewhat confusing and redundant. In the first sentence, it states that the awardee must track the affordable housing only to the extent it was financed with the CMF award. The second sentence further delineates that the awardee need only track the 10-year affordability requirements for those housing projects funded with CMF dollars. *We would recommend dropping the second sentence altogether, since presumably the first sentence is already written in a broad enough manner to encompass the fact that awardees are not required to track the 10-year affordability requirements in the case of housing not financed with CMF award dollars.*

Section 1807.302. Restrictions on the use of a CMF Award. 1807.302(c) states that "In any given application round, no more than 30% of a CMF Award may be used for Economic Development Activities." In order to maintain the flexibility to adjust this figure (either upwards or downwards) in future rounds, the CDFI Fund may want to set such limitations in the NOFA, instead of in the regulations. *We would recommend striking and replacing this sentence with "In any given application round, the CDFI Fund shall specify the percentage of a given CMF award which may be used for Economic Development Activities."*

Section 1807.303. Authorized Uses of Program Income.

1807.303(a) is helpful in that it clarifies that principal and equity repayments are required to be reinvested in CMF-eligible activities for the duration of the 5 year award period. However, with respect to awardees that did not intend or do not otherwise need to pursue a reinvestment strategy in order to meet the terms of their assistance agreements (e.g., with respect to meeting the leveraging requirements), *the CDFI Fund should provide further clarification (if not in the regulations, then in the assistance agreement or any accompanying guidance documents) as to the awardee's requirements with respect to reporting this information to the CDFI Fund.* Should it be reported as if it was a "CMF transaction"? If so, is the awardee then obligated to meet all of the compliance requirements (e.g., the 10 year affordability requirements, the deeper targeting requirements) as if this was one of the awardees "initial" CMF transactions? This

would be unnecessarily onerous to the CMF awardee and, furthermore, would not be consistent with the intent of the statute, which is to provide institutional level investments for CDFIs and non-profit housing organizations.

1807.303(b) governs how interest income is to be treated. It includes a reference to 2 CFR Part 1000, which itself then cross references 2 CFR Part 200, of which only portions of that section apply to interest income. To ease the burden on awardees and help ensure better compliance outcomes, the CDFI Fund should provide separate written guidance on the allowable use and deployment of interest income.

Section 1807.401. Affordable Housing – Rental Housing

Section 1807.402(d) states that affordability requirements apply must be imposed by deed restrictions, covenants running with the land or other recordable mechanisms. Given the alignment of this program with the Low Income Housing Tax Credits projects, *we recommend clarifying language be added to this section such that Recipients may satisfy the requirement for such deed restrictions or covenants by the recording of LIHTC affordability restrictions and covenants, provided that the Recipient has a mechanism for monitoring compliance.*

Section 1807.401(f)(4) states that “The CDFI Fund reserves the right to deem certain government programs, under which a Low Income Family is a recipient, as income eligible for the purpose of meeting the tenant income requirements under this section.” *We encourage the CDFI Fund to provide more detailed information in its subsequent compliance monitoring guidance materials indicating which programs may be applied as proxies, as well as what records need to be retained by the awardees.*

Section 1807.401(g)(3) addresses replacement of vacancy with a tenant that meets the affordability qualifications for the same income category of the original unit. *We propose deletion of the “same income category” requirement and instead suggest: “If there is not an available replacement unit, the Recipient must fill the first available vacancy with a tenant that meets the affordability qualifications as necessary to maintain compliance with the CMF requirements and the Assistance Agreement.”* We believe that this might offer more flexibility, and allow for a unit not to remain vacant for too long.

Section 1807.500. Leveraged Costs, Eligible Project Costs. Section 1807.500(c) requires that “recipients maintain appropriate documentation, such as audited financial statements, wire transfer documents, pro-formas, and other relevant records” to demonstrate the receipt of leveraged sources of funding. *The CDFI Fund should clarify, either in the regulations or in subsequent guidance, whether the recipient is required to maintain all such documents, or if any single document among those listed will be sufficient, provided that it demonstrates on its own that (depending on the timing) that the leveraged funds are anticipated, committed, or have been received.*

Section 1807.503. Project Completion. Property Standards.

Section 1807.503(a) indicates the conditions that must be met with respect to deeming that a project has been “completed”. These requirements seem subjective and at the determination of the CDFI Fund, when the CDFI Fund, from a practical standpoint, would not be involved in each individual project to determine whether conditions were met to deem a project as having been “completed”. It would be better to identify more uniform standards, such as a certificate of occupancy. *We suggest that the opening clause of Section 1807.503(a) also be restated as follows: “Upon Project Completion, the Project must be placed into service by the date designated in the Assistance Agreement. Project Completion occurs, as determined by the CDFI Fund, when:...” [with objective criteria set out in enumerated subparts].*

Section 1807.503(a)(4) includes a distinction pertaining only to preservation deals. It is not clear why there needs to be a special provision pertaining to preservation deals when they must already meet the first three provisions contained in this section. *We recommend that the CDFI Fund strike Section 1807.503(a)(4).*

Section 1807.503(b)(3)(i) places a requirement on the Recipient to ensure that at Project Completion, the developer or Project Sponsor establishes a replacement reserve and that monthly payments are made to the reserve that are adequate to repair or replace the systems as needed. This requirement is too onerous, particularly when the Recipient is providing early (e.g. predevelopment) funding, it is neither feasible nor practical for the Recipient to dictate reserve requirements. Moreover, it may be unclear or debatable as to what may constitute “major systems” for which a replacement reserve needs to be established. *We suggest that this section be changed such that the Recipient merely be obligated to confirm that permanent financing requirements include a requirement for the establishment of adequate reserves: “For rental Housing, the Recipient shall communicate a requirement to the Project Sponsor or the developer for the establishment of adequate reserves for the replacement of major systems necessary for the habitability of the Project and confirm that any permanent financing requirements for such Project include the establishment of adequate reserves.”*

Section 1807.902. Data collection and reporting. This section is extremely broad and open ended, which might be sufficient for the purposes of the regulations. *However, at such time as the assistance agreement is developed, the CDFI Fund should provide much more detail about what kinds of information must be retained with respect to all aspects of reporting and compliance monitoring, with an eye towards only requiring the awardee to maintain information that is essential for the purposes of demonstrating compliance and/or program outcomes. We also recommend adding a clarification in Section 1807.902(b) that data may be retained or collected on an aggregated, de-identified basis, to avoid issues of potential compromise of personally identifiable information of program end-beneficiaries.*

OTHER RELATED COMMENTS

Leveraging Requirements. LISC generally supports the efforts of the CDFI Fund to “drive” applicants to achieve better impacts by having them commit to outcomes above and beyond the

minimum statutory or regulatory requirements, as the CDFI Fund has done in the 2016 CMF round with respect to encouraging applicants to target very low-income populations; serve areas of high housing need; etc. To this end, it was a little surprising that the CDFI Fund did not also include incentives for organizations willing to demonstrate leverage beyond the 10:1 minimum statutory requirement, given that this is probably the single most defining characteristic of this program. Instead, the CDFI Fund explicitly advised applicants that they would not receive credit beyond the 10:1 ratio required in the statute.

While we appreciate that “project level leveraging” can certainly drive up this ratio significantly (e.g., when an awardee makes a predevelopment loans that is only a tiny fraction of the project’s total costs) and should be viewed differently than the more difficult to obtain pre-investment leverage funds, it is nonetheless important to reward leveraging at all points and to encourage applicants to go above the statutory minimums, within reason. The 2010 CMF round effectively capped the credit an applicant would receive in the scoring at 20:1, primarily because it also included an incentive for awardees to finance at least 5% of any given property’s total project costs. This was done to provide a “check” against over-inflation of the leveraging figures by applicants. We assume that there was good reason for the CDFI Fund to take the 5% requirement out of the application, and we are not arguing for its re-insertion. *We are simply suggesting that the CDFI Fund revise its guidance for future rounds to allow awardees that are leveraging beyond the minimum 10:1 ratio to get some extra consideration for these efforts – even if it is capped (e.g., at 15:1 or 20:1).*

A related issue that needs to be addressed prior to the issuance of this year’s allocation agreements is how the percentage of private sector investments will be measured with respect to organizations that exceed the 10:1 leveraging thresholds. The CDFI Fund will likely discover, when it receives the project level reports, that many awardees will be producing total leveraging ratios of 20:1 or greater, driven primarily by total eligible projects costs at funded projects. Some of the leveraged dollars beyond the 10:1 will no doubt be coming from public sources (e.g., HOME funds, contributions from local governments). Will these contributions “over and above” the 10:1 leveraging ratio then count against the organization’s percentage commitment to secure private sector leveraging? Because it strikes us as inconsistent to on the one hand to advise an organization that it cannot get credit for leveraging beyond the 10:1 ratio, and then on the other hand penalize it by counting the public contributions from this same “additive” portion of leveraging.

Example: An awardee receives a \$1 million CMF award. By statute, it must use this award to support at least \$10 million in total eligible project costs (10:1). Its award agreement further requires the awardee to fulfill a pledge in its application to ensure that 80% of its leveraged capital would come from private sources. The awardee uses its CMF award to attract \$1 million from a private bank, and then utilizes the \$2 million in blended capital to make investments supporting total eligible project costs of \$20 million (20:1 leverage), of which \$5 million came from public subsidies (inclusive of the \$1 million CMF award), and \$15 million came from private sources (inclusive of the initial bank loan of \$1 million). If the applicant were reviewed based on the total eligible project costs of \$20 million, the applicant would fail because only 75% of the total eligible project costs are attributable to private sources. However, if the review was done in a manner to ascertain that at least 80% of the \$10 million in “required” leverage (or

\$8 million) is supported by private capital, then the awardee would pass this requirement, since a total of \$15 million (150%) will have come from the private capital.

Application Consistency. As stated above, we applaud the CDFI Fund's efforts to drive better outcomes by incentivizing applicants to achieve outcomes above and beyond what is minimally required by statute and regulation. However, the CDFI Fund needs to ensure that it pursues a balanced approach, and provide applicants with sufficient narrative opportunities to explain their overall strategies in cases where they may not be achieving the numeric targets that the CDFI Fund is attempting to drive them towards. For example, in the 2016 CMF application, an applicant that commits that a significant portion of the funds will address very-low and extremely low income populations will be scored more favorably. This information is captured in Q.22 of the application. Yet in Q.23, the CDFI Fund then asks what efforts the applicant will make to finance mixed income developments, which while a laudable outcome and one that should be encouraged, is inconsistent with the strategy of deep targeting favored by the CDFI Fund in Q.22. Similarly, in Q.21, an applicant is encouraged and will be scored more favorably for serving neighborhoods of high housing need. However, these neighborhoods are generally not the "mixed income communities" which applicants are then asked to discuss in Q.23.

We thank you for this opportunity to provide comments.

Sincerely,

A handwritten signature in blue ink, appearing to read "Matt L. Josephs", with a long horizontal flourish extending to the right.

Matt Josephs
Senior Vice President for Policy