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Coalition of Lenders and Investors Help Create the Community Development Financial Institution Act of 1994

By Mark A. Pinsky

When more than 500 hundred people met for the Community Development Financial Institution (CDFI) Training Institute in Durham, NC, in late January, 1994, participants called this first official gathering of the emerging CDFI industry "CDFI Woodstock."

The CDFI industry reached an even more significant milestone on September 23, 1994, when President Clinton signed the CDFI Act of 1994. The act created the CDFI Fund, an independent federal agency designed to support and expand the network of more than 300 CDFIs in the United States. To a remarkable degree, the fund was shaped by the experiences of CDFI practitioners in urban and rural communities across the nation, working through the CDFI Coalition.

Since it formed on November 20, 1992, the CDFI Coalition has brought together diverse community development lenders and investors, articulated the industry's vision for a federal program to support the field, and become the primary source of information for Clinton Administration and Congressional staff members working on the CDFI Act as it wound through Congress.

Beyond South Shore

In late summer 1992, then-candidate Bill Clinton announced during a campaign stop outside South Shore Bank in Chicago that, if elected, he would establish a program to create 100 community development banks modeled on South Shore, as well as 1,000 micro-enterprise lenders. As a campaign promise, the idea caught on.

When candidate Clinton became President-elect Clinton, Martin Paul Trimble, former executive director of the National Association of Community Development Loan Funds, and Cliff Rosenthal, executive director of the National Federation of Community Development Credit Unions, convened a meeting of industry leaders. They wanted to work to ensure that as the campaign promise became legislation it would reflect the cumulative experience of seasoned practitioners. Because the industry had previously avoided public policy, participants in the meeting had low expectations. In fact, the CDFI Coalition formed as a defensive action, to prevent the community development banking bill from ignoring the range of community development finance intermediaries. Yet the nascent CDFI Coalition had already begun building its foundation years earlier.

In the mid-1980s, Rosenthal had written a visionary paper, proposing a National Neighborhood Bank, that anticipated not only President Clinton's CDFI idea but many of the key controversies that would emerge. In 1992, Trimble, Rosenthal, and a small group met several times at Trinity Church in Manhattan to bat around policy ideas. The concept papers drafted by the "Trinity Group" later proved valuable to the Coalition. In addition, in 1992 Congress approved an amendment to major housing legislation that set up a small program foreshadowing the CDFI Act of 1994. The 1992 demonstration legislation, which was never funded, had stronger Republican than Democratic support, as conservatives saw CDFIs using creative business methods to meet housing and economic development needs.

Today the Coalition's 310 CDFIs in 45 states manage more than $1 billion in capital, the vast majority from private sector sources such as banks, religious institutions, and individuals. Coalition members have loaned more than $3 billion, with aggregate loan loss rates competitive with the best banks.

The Coalition had a far greater influence than any of its individual sectors might have had alone. Having CDFIs in 45 states proved critical, providing a geographically broad constituency. Having a "b" rather than an "m" before the "illion" added credibility to the industry, even though collectively it is about the size of a small bank. The loan loss rate reflected the labor-intensive work CDFIs do to mitigate risk and affirmed that CDFIs are serious financial institutions that meet their responsibilities to investors. The CDFI industry's strong performance track record, demonstrated both in financial statements and in the improvements in the lives of hundreds of people from rural Maine to South Central LA, made its practices a strong model for the federal legislation.

The Coalition hammered out a concept paper, which it issued in late January 1993 as "Principles of Community Development Lending & Proposals for Key Federal Support." No one involved in drafting the paper anticipated the major impact it would have, in part because everyone underestimated the policy vacuum on this issue.

The "Principles" paper set out an aggressive vision for what federal support for the CDFI industry might entail. Underlying the principles was the quietly radical idea that the federal government could appropriately support CDFIs, which specialize in leveraging conventional capital into communities, rather than concentrating on project-based support.

In December 1992, the Coalition shared drafts of the principles document with congressional aides and participated in a series of discussions organized by the Senate Banking Committee staff. In what turned out to be its most important move, several Coalition members late one afternoon took a working draft of the document to the Clinton transition headquarters, even though no one knew who on the transition team was working on the issue. A small group waited several hours before a junior aide emerged only long enough to say that he would not be able to meet with the group that night. After shoving a copy of the paper into his hands, one of the Coalition members offered to stay overnight in Washington and to meet with the aide over breakfast. The aide met the next morning with a small group of Coalition representatives.

The Coalition had no further contact with transition staff and anticipated little response. A newspaper story in early January 1993 erroneously reported that the President would propose a $1 billion budget for his community development "banking" proposal. The first indication that the transition team was heeding the Coalition's counsel came when President-elect Clinton said, during an MTV special, that he would propose the creation of a national network of CDFIs.

The Senate Banking Committee scheduled a hearing for February 3, 1993, and invited several Coalition representatives to testify. On a lark, the Coalition asked Senate Banking Committee Chairman Don Riegle to host a Coalition-led briefing the afternoon prior to the hearing. Riegle sent a letter to congressional staff in late January, and when Coalition members arrived at the Senate Banking Committee hearing room on February 2, they found a crowd of several hundred people from Capitol Hill, the Administration, the Federal Reserve, and the media. Coalition members began to think that they might have their say after all.

The Coalition firmly believed that hiring a lobbyist ran counter to the values of community-based organizations, yet it had few resources and knew that it would get rolled if it tried to stand toe-to-toe with banking industry lobbyists, who were vying to make the program fund their activities. Coalition members knew they could succeed only by having CDFI practitioners make the case in the communities where they lived and worked.

The first effort to explain CDFI work in communities brought three key Senate Banking Committee staff members to North Camden, New Jersey; Philadelphia and New York City in January 1993 to meet with CDFI borrowers and lenders. That experience showed the Coalition that this approach would work if it got strong enough community participation. In the words of one Coalition representative, "When you get people from DC into these communities, they get our religion and become our best supporters."

In April, the Coalition arranged its first of many meetings with White House aides. Two main factions within the administration were debating the structure of the president's proposal. One side favored the CDFI Coalition approach, while the other wanted to use federal funds to encourage banks and other conventional lenders to step up their lending in underserved communities. But the extensive public commitments the administration was making to "bottom-up" solutions at the time seemed to work to the Coalition's advantage.

As the administration prepared for the president to outline his proposal at a July 15, 1993, White House event, the Coalition focused on several primary organizing challenges.

Industry Identity

Pulled together abruptly and with a sense of urgency, the Coalition wanted to develop an industry identity and get on the radar screens of a mix of people in the administration and on Capitol Hill. Coalition members strove to allay skepticism over the legitimacy of CDFIs, outsiders inside the beltway. Perhaps the Coalition's most effective strategy to gain legitimacy in Washington was its practice of reaching elected officials in their home districts or states. The CDFIs operating in more than 45 states proved an enormous, if coincidental, benefit.

Coalition members also worked to ensure that Washington-based advocates for the Community Reinvestment Act (CRA) and for community-based development understood the Coalition's goals and its general support for programs that improved access to capital in underserved, distressed, and disinvested communities. Early on in the legislative process in 1993, opponents of the president's plan had unsuccessfully tried to pit CDFIs against the CRA.

In its organizing, the Coalition also distributed materials explaining what CDFIs are and how they work. A list of CDFIs was compiled for anyone asking for information. And the Coalition produced a CDFI "primer" that explained how CDFIs balance financial and social returns on their investments. Because an information gap existed on this issue, the Coalition was able to position itself as the information source, allowing it to develop a substantial mailing list and to influence the information flow over time. The Coalition later also started a two-page monthly newsletter.

While the Coalition organized, its members identified five key issues they wanted the legislation to address.

First, the Coalition persuaded administration and Congressional leaders that eligibility for the CDFI program should exclude conventional financial institutions and their subsidiaries, such as bank CDCs. If the program were opened to these institutions, CDFIs would be effectively shut out. The Coalition explained that CDFIs are capital-starved organizations that would be able to significantly expand their financing capacity under a federal program, while using taxpayer money to support conventional lenders would produce no added "bang for the buck."

In addition, Coalition members argued that local market conditions should dictate the structure of CDFIs, whether depository, such as banks and credit unions, or non-depository, such as loan funds and micro-enterprise lenders. The Clinton Administration had originally tilted the CDFI playing field to favor depositories over non-depositories. Coalition members pushed for policies to discourage that bias.

The Coalition also wanted to ensure that the CDFI program did not become just another government bureaucracy. It urged that an independent agency, governed by a board with true supervisory authority, run the program.

Another important condition the Coalition wanted the legislation to include was that the program concentrate on building strong CDFIs, rather than on project-oriented financing.

Finally, the Coalition knew that equity, or net worth, capital was the major need of most CDFIs and asked legislative drafters to ensure that the CDFI program emphasized this type of support, though not to the exclusion of operating support and long-term, low-cost debt.

CDFI Act Implements Principles of Community Development Lending

The final version of the CDFI Act of 1994, which passed the Senate unanimously and the House by a 410-12 vote, largely implements the vision articulated by the CDFI Coalition in 1993 in its "Principles of Community Development Lending." The CDFI Fund created under the act provides equity, debt, operating grants, and training support to expand the established network of CDFIs and to support new CDFIs in select markets. It allows eligible institutions to apply for up to $5 million per institution over three years – with no significant preference for depository CDFIs. It uses a performance-based financing system. It emphasizes local community accountability and control.

The CDFI Act has already fundamentally changed the way CDFIs see themselves. The credibility CDFIs have gained from extensive national attention has helped some institutions increase their fundraising and has opened many new doors. Some CDFIs, for example, have found partners in banking and municipalities. And even Federal Reserve Board Chairman Alan Greenspan gave a nod to the CDFI industry in a 1994 speech.

Congress appropriated $125 million for the CDFI Fund's first fiscal year, which began on October 1, 1994, and the Clinton administration has begun hiring staff for a transition team to help set up the CDFI Fund. It has also narrowed its choices for a fund administrator and expects to nominate its choice in early 1995. At the soonest, the Fund might issue a request for proposals by early summer and disburse funds by the end of the fiscal year on September 30.

Assuming that it survives the budget cutting of the new Congress, the CDFI Fund will significantly expand the capacity of CDFIs to serve distressed and disinvested communities. CDFIs in places as diverse as the Pine Ridge Indian Reservation in South Dakota; downtown Baltimore, Maryland; and Washington State's Olympic Peninsula have begun to exert what one industry leader calls their "institutional egos" and have demanded that private and public policy makers respect them and serve the neglected markets they represent. Because CDFIs are both models for and challenges to conventional capital sources, this combination of organized money and organized people holds significant potential.

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