

PENNSYLVANIA LOW INCOME HOUSING COALITION

2 SOUTH EASTON ROAD • GLENSIDE, PA 19038 • (215) 576-7044
2 GATEWAY CENTER, 18TH FL. • PITTSBURGH, PA 15222 • (412) 281-2102

Testimony of the Pennsylvania Low Income Housing Coalition on S.B.10, the
Community Development Bank Grant and Loan Program

Daniel Hoffman, Policy Director

Introduction

Mr. Chairman, members of the Commerce and Economic Development Committee, on behalf of the more than 200 member organizations of the Pennsylvania Low Income Housing Coalition I want to thank you for holding this hearing and thank you in advance for considering the comments that you will hear from all of today's witnesses as part of your legislative deliberations on this important bill.

During the past few years there have been a number of significant changes in the state's housing and community development landscape. Among these changes have been the demise of the Department of Community Affairs and its replacement by the less housing oriented Department of Community and Economic Development. Within DCED we have witnessed changes in funding priorities resulting in decreased support for affordable housing including the diversion of Housing and Redevelopment program funding for economic development purposes. The state still lacks a dedicated source of funding for housing including funds to match the federal HOME program. Meanwhile, the Housing Finance Agency continues to administer a self-limited set of programs in ways that do not seek to focus its resources on distressed communities or on consumers most in need of housing.

So when we heard the Governor announce his support for a community development bank, we hoped that this would be an important signal of a renewed interest in housing. The Pennsylvania Low Income Housing Coalition believes that community development banks can be an important instrument for community revitalization. Our members have worked with community development banks both as borrowers and as part of the community-driven lending process that is the essence of community development banking.

Unfortunately, as we read through the Administration's briefing materials and heard additional comments we came to recognize that our membership was to be excluded from the state development bank, both as a borrower and as a participant in the lending priority decision-making process. Conversations with Administration officials in which we sought to have them model their proposal on the successful federal legislation proved to no avail and led us to come to the legislature which to date has been responsive to our concerns by not granting the Governor a blank check for this bank in the state budget and now by holding this hearing on S.B. 10.

Before discussing the three concerns that our organization has I want to take a moment to make one important, but general, point. Community development lending is tough to do. If it was easy large banking institutions would have figured out how to do it and none of us would be here today. Key to successful community development banking is creativity and flexibility. The legislation that you ultimately pass must acknowledge this. We would not want to have legislation that so micro-manages this program that the creativity and flexibility that has marked the work of community development banks in this state and throughout the nation is lost or even lessened. Indeed, we believe that the resolution of each of our concerns leads to a program that is more flexible, more inclusive and provides more options for communities to take charge of this program and their futures.

Three Needed Amendments

The first concern that we have is that this proposed bank would be the only community development bank in the nation with no housing mission.

Housing rehabilitation and development is a key component of community revitalization. It is not the only component. Certainly job generating strategies are vital. What communities require and what S.B.10 needs is a balanced approach to community development.

The Administration has said that the balance to S.B. 10 is the Housing Finance Agency. This comment either reflects a profound misunderstanding of the agenda of PHFA during this administration, or is simply disingenuous. PHFA has no housing rehabilitation programming, does not have programming that targets underinvested or blighted neighborhoods and spends few state or federal discretionary dollars on multi-family housing. Nor has the Agency been a leader in helping to expand local community loan fund programs as housing agencies in other states have been.

PHFA could be the “balance” to this community development bank proposal, but it is not and the current agency leadership has no intention of making it such an agency. Therefore, it is the community development bank that must be positioned to be the leader in revitalization.

Frankly, we think this could be done with three simple provisions. First, recognizing the relatively limited amount of money being devoted to this program, the bank should focus on strategically important housing that is linked to economic development and revitalization. The bill should specifically authorize redevelopment financing for what downtown advocates sometimes refer to as “upstairs, downtown;” the restoration of frequently abandoned, deteriorated and obsolete space above first floor retail in many older downtowns, in large communities and small. Many studies have shown that persons who live downtown spend much more money downtown than those who simply office there. Enabling this under-utilized upper story space to become useful housing will bring new customers to the businesses that this bill is trying to create.

Specific legislative authority for this type of lending would re-enforce “MainStreet” programs throughout the state. I believe that this committee has received correspondence from the Pennsylvania Downtown Center which works with MainStreet programs throughout the state endorsing this concept.

A second housing related amendment we seek would specifically authorize the conversion of abandoned and obsolete office, commercial and industrial and other institutional space for housing purposes. Again the existence of this blight deters economic development and the state has no other targeted efforts to finance the conversion of these symbols of decay into new homes and new neighborhoods.

Thirdly, you could require local CDFIs to have a housing plan and to take meaningful steps to accomplish that plan. This would require CDFIs to go out and seek other sources of funding and work with communities to improve housing conditions as a condition of being eligible for state CD Bank funding even if the state funds were not used for housing purposes. In this way, the state’s efforts to catalyze a CD banking industry via technical assistance grants, a feature of the proposal that we wholly support, can also be a feature that serves to expand housing opportunity. Requiring such a plan is part of the federal law and application process for those local CDFIs seeking access to federal Community Development Financial Institutions Act funds. The state CD Bank law should have a similar requirement.

With these amendments the legislature would be; a) specifically informing the executive branch that housing is to be part of the state’s community development strategy; b) limiting the financial drain of housing costs on this relatively small program; and, c) encouraging emerging local CDFIs to become engaged in housing issues.

A second concern that the housing coalition has relates to the governance of this entity. Key to the success, indeed the essence of successful community development banking, are the linkages between the community and the banking functions. In this area the Administration’s proposal is woefully lacking. The bank is to be housed in the Pennsylvania Economic Development Finance Authority (PEDFA). PEDFA, an agency that floats bonds and disburses money to business is undoubtedly a fine organization, but it has no record of working effectively in low income communities. Indeed, this agency is essentially unknown in low income communities. The bill authorizes PEDFA to, at its discretion, establish an 11-member committee, including the Secretaries of DCED and Banking, which may have full operational power over the program. The other nine individuals are to represent investors and other members of the general public. These members will serve at the pleasure of the PEDFA board. From the briefing paper that the Administration has prepared it would seem that the Administration views this to be a board of bankers, utility and insurance companies and the like. Indeed, planning meetings among Administration and banking officials have already begun. The Administration’s briefing paper speaks of establishing an investment and loan committee dominated by large business interests that would set the bank’s policies.

This is not community development banking. Community development banking includes communities and communities are missing from this proposal.

Again, the federal CDFI law is instructive. For a variety of reasons, the governing of the federal program is left to the Treasury Department, but an advisory board to the Treasury was established. Like the Administration proposal, the federal board includes nine members of the general public. Each of these members serves for a 4 year term to provide them with some degree of independence. Moreover, the federal legislation requires that these Presidential appointees include 2 persons from community development financial institutions, 2 persons from insured depository institutions, 2 persons representing consumer and/or public interest organizations, 2 persons with expertise in community development and 1 individual with knowledge of Native American communities. The legislation also requires that attempts be made to balance the board in terms of geographic, racial, ethnic and gender diversity.

State law should do no less. The legislature can and should ensure that representatives of low income communities, including rural communities, play a leading role in policy-making and priority setting. The state CD Bank leaders should not simply be a collection of individuals representing institutions that have already demonstrated that they have limited ability to successfully serve neighborhoods in need. This Committee should amend S.B. 10 to ensure that knowledgeable representatives of low income communities have a substantial and independent role in the governance of this important new institution.

Our final concern goes to the heart of the Governor's proposal. Let me reiterate, the Pennsylvania Low Income Housing Coalition is for community development banking. We are here today for two reasons. First, we want our members to be served by and participate in this new entity. Second, we want this proposal to work. We are concerned that as currently structured the Administration proposal may not work. And even if it might, clearly the way in which the Administration proposes to use the \$10 million appropriated is not an optimal use of scarce funding. We urge you to give this and/or future administrations the ability to use this funding in a smarter, more strategic ways.

The heart of the Administration proposal is to blend its \$10 million with \$30-\$50 million from the private sector. This is a lot of leverage. As a result, unless the private sector makes very deep concessions the interest rates offered are likely not to be all that attractive. Indeed, it may well be that even if limited housing deals are permitted there will be very few of them because the cost of money is simply too high.

But there are two more central problems. First, and this relates to the governing structure of the proposal, previously discussed, we believe that the influence given large corporations, particularly lenders, will result in this program looking more like a bank partnership program than a CDFI. Bank partnership programs were tried during the 1980s and were of limited success because each participating lender was given a voice in loan underwriting. Lenders had trouble agreeing on common underwriting criteria and as a

result it was difficult for bank partnership programs to actually make loans. CDFIs, which increase the involvement of communities and decrease the voice of individual lenders, came into being in order to overcome the failures of bank partnerships. The large role given lenders in the governing of this program and the limited consideration given to community participation, raises the specter of another bank partnership flop.

Our second concern is that funds would be lent from the state bank to local CDFIs. Because money is being lent to local CDFIs, the program will do little to grow the asset bases of the local banks. The only money that the local CDFI will make on the state money will be transaction fees and interest charges. Moreover, local CDFIs will be forced to compete, at a disadvantage, for lender participation in their local lending programs as lenders will prefer to participate in the state program rather than in local programs.

This will be particularly problematic when a local CDFI wants to use funds deposited by a lender for a loan that the lender has already participated in via the state bank. Lending risk for a bank will not be lessened by leveraging funding lent to the state program against their own funds lent to local CDFIs. Loans will get “one bite at the apple” and that bite will be through the state program and come at the expense of local CDFIs.

Perhaps some of this problem is solvable with regional lending pools. And perhaps the administration can make lenders, non-depository financial institutions, utilities and the like participate in this program, at least one time. It would be good if they could and if this participation did not detract from local CDFI programs.

In fact there is some utility in challenging the private sector to participate in community development as proposed, even if that reason is to prove to state leadership that the private sector will not make the investments that are needed and that therefore additional public resources are needed. We do however, remain skeptical on the private sector’s participation and urge you to amend this bill to provide flexibility for this program to function even if the private sector’s participation is more limited than the Administration predicts.

Alternative Programming Strategies

We thus close with four suggestions regarding alternative ways of configuring the state bank to spur development, build local capacity and more effectively use scarce state resources.

One way in which state funding might be used is to simply make equity investments in local or regional CDFIs. CDFIs are good at leveraging their funding, know the local community and its lending needs and are chronically short of funds to lend. By simply granting CDFI’s funding they can achieve the economic mission of the state bank

without a lot of state bureaucracy and committees. Equity infusions will do more to make local CDFI programs grow than what is being proposed. In contrast, the proposed program will make the local CDFIs mostly a pass-through entity, with loan repayment profits returned to the state rather than to local communities.

A second way in which the state funds might be creatively used would be as a secondary market, buying loans and participations in pools of loans generated by local CDFIs. Creating a secondary market for loans that lack a secondary market would add tremendous liquidity to the network of CDFIs that the state proposes to establish.

Third, the state could use the \$10 million appropriated for the bank to partially guarantee or insure a \$100 million tax-exempt Housing and Industrial Revenue Bond issue. This would enable the bank to; a) lend sufficient funds for larger, community-changing projects; b) do more deals; c) put more money into each deal, lowering the blended interest rate charged by the public and private lenders; and, d) be of sufficient size to command the attention of the lending community and signal to local CDFIs that this program has staying power.

Fourth, the state could lend no money, but rather capitalize an insurance program to back commercial and industrial mortgages. Similarly, the state could expand the powers of the PHFA mortgage insurance fund to enable it to be a force for urban and rural revitalization, which its charter does not currently permit. There is little evidence of a capital shortage in Pennsylvania, but there is an unwillingness to invest in disinvested communities at affordable rates. By providing a risk hedge the state could make capital acquisition in disinvested communities more affordable. Tomorrow, in Lancaster, your counterparts on the Urban Affairs committee will be holding a hearing on just such a bill. I would hope that this committee would coordinate its legislative activities with the Urban Affairs committee so that we gain a coordinated, strategic and innovative approach to countering the problems of disinvestment.

It is good that the Governor put community development lending on the agenda and the proposal to facilitate a statewide network of local community development banks is an excellent idea.

In making this proposal it would have been better if greater attention had been paid to learning the lessons of community development banking in this state and across the nation. Three of those lessons: that providing desirable, affordable housing is a key ingredient in community revitalization; that the significant involvement of low income communities in community development lending is essential; and, that state funds should be used to strategically assist, not supplant, local efforts can yet be incorporated into this proposal. The Pennsylvania Low Income Housing Coalition urges all of you to support amendments to incorporate these lessons into the proposed legislation before you.

Thank you for the opportunity to share these thoughts with the Committee.