

BANKING ON THE FUTURE:  
THE ROLE OF BANK COMMUNITY DEVELOPMENT CORPORATIONS  
IN COMMUNITY DEVELOPMENT

BY  
Bridget Letticè Ware

B.A. University of Maryland- Baltimore County  
1987

Submitted to the Department of Urban Studies  
and Planning in partial fulfillment of the requirements  
of the degree of

MASTER IN CITY PLANNING

at the

MASSACHUSETTS INSTITUTE OF TECHNOLOGY

May 1989

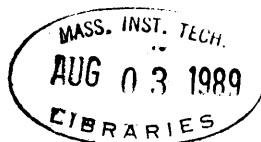
(c)Bridget Letticè Ware

The author hereby grants to M.I.T. permission to reproduce and to distribute copies of this thesis document in whole or in part.

Signature of Author \_\_\_\_\_  
/ ~ Department of Urban Studies and Planning  
May, 1989

Certified by \_\_\_\_\_  
Phillip L. Clay  
Associate Professor, City Planning  
Thesis Supervisor

Accepted by \_\_\_\_\_  
Donald Schon  
Chair, MCP Committee



Rotch

BANKING ON THE FUTURE:  
THE ROLE OF BANK COMMUNITY DEVELOPMENT CORPORATIONS

by

Bridget Letticè Ware

Submitted to the Department of Urban Studies and Planning  
on May 23, 1989 in partial fulfillment of  
the requirements for the Degree of Masters in City Planning

ABSTRACT

In recent years community and economic development issues have become the focus of an increasing number of banks. Bankers realize that an important component of survival and profitability is link to the economic well being of the community they serve. A bank's link to the community goes beyond merely receiving deposits and providing customer account services. Banks play a key role in maintaining stable communities through various community economic development mechanisms.

One way an increasing number of banks have sought to facilitate community economic development on a long term basis is through the creation of bank community development corporations (CDC). Bank CDCs are a private initiative through which banks can exercise leadership in and demonstrate long-term commitment to community development.

This thesis presents case studies of three models of bank CDCs-- Black Business Investment Corporations, North Carolina National Bank CDC, and Chemical Community Development, Incorporated. This thesis addresses two questions: 1) What factors are critical to a bank CDCs organizational development and ability to achieve its goals? and 2) Based upon these critical factors, what are criteria for assessing the bank CDC model's influence on community and economic development?

The case studies illustrate that three elements play a critical role in bank CDC development ability to achieve goals: strong support and sponsorship of a parent bank and staff, good relations with communities and public sector actors, and a thorough understanding of community credit needs. The thesis concludes with suggested criteria which regulators should implement in beginning to assess the impact of bank CDCs.

Thesis Supervisor: Dr. Philip Clay

Title: Professor of City Planning

## TABLE OF CONTENTS

<b>CHAPTER 1: INTRODUCTION .....</b>	<b>5</b>
<b>CHAPTER 2: THE CONTEXT FOR BANK CDCs</b>	
Rationale for a Bank CDC.....	14
Risks.....	16
Comparison of Bank CDC and Traditional CDC.....	17
Bank CDC Regulations.....	18
Bank CDC Models.....	23
Bank CDC Structure.....	27
 <b>PREFACE TO CASE STUDIES.....</b>	 <b>35</b>
 <b>CHAPTER 3: BLACK BUSINESS INVESTMENT CORPORATIONS</b>	
Case Study.....	37
Analysis and Comment.....	44
 <b>CHAPTER 4: NORTH CAROLINA NATIONAL BANK CDC</b>	
Case Study.....	48
Analysis and Comment.....	53
 <b>CHAPTER 5: CHEMICAL COMMUNITY DEVELOPMENT, INC.</b>	
Case Study.....	57
Analysis and Comment.....	61
 <b>CHAPTER 6: CONCLUSION.....</b>	 <b>64</b>
 <b>BIBLIOGRAPHY.....</b>	 <b>77</b>
 <b>APPENDICES.....</b>	 <b>80</b>

## ACKNOWLEDGEMENT

First, I would like to thank the Creator, through whom all things are possible. The cast characters who have helped through these last two years is a long list. To my reader and boss, Jim Carras, I would like to express my gratitude and appreciation. To my friends/therapists Laura, Marina, Renae, Anne, and Alex I would like to express my thanks for their: flexibility, patience, **ADVICE**, food, and humor which to kept me from falling off the edge.

To my friends, near and far, who were just a telephone call away (you know who you were), Your advice and direction was always welcomed and always on time. Finally, to my mother and sister, I owe love and gratitude for everything.

## Chapter 1 INTRODUCTION

### WHAT IS A CDC?

The term "Community Development Corporation" (CDC) is traditionally applied to the nonprofit, grass roots organizations which emerged around urban centers during the 1960's as a result of the crises experienced in these areas. The historic neglect and deterioration of urban centers created an explosion of rioting and violence during this period. From this tumultuous period, CDCs emerged as vehicles to empower communities. CDCs, usually nonprofit organizations, were designed to empower and enable neighborhood residents to carry out their own comprehensive programs of local renewal activities. They took on various projects including providing working capital to small and minority-owned businesses, developing employment services programs, and providing physical improvements such as landscaping and streetscaping to neighborhoods. However, pursuing these activities requires continuous operational and administrative funding.

Communities, especially inner-city, low-income communities, face a multitude of problems which require more funding than CDCs can garner from community donations only. To begin to address the wide ranging needs of communities as well as meet operational costs, CDCs must seek donations, grants, and loans from public and private sources.

In the past, CDCs were able to take advantage of a vast array of governmental programs "to invest in their communities, and they found increasing support from private foundations and lending institutions." <sup>1</sup> Today the levels of support from private foundations and lending institutions is often conditional on government funds being available to the CDC. In light of diminishing government funding for programs for community economic development, funding for operational and project support has become more difficult.

A decade of the Reagan Presidency saw sharp cut backs and the dismantling of a multitude of programs CDCs traditionally looked to for funding. A recent Ford Foundation report enumerated some of the more dramatic changes and succinctly summarized the current trend for CDCs:

"The federal Community Services Administration, major funder of CDCs, is dismantled. So is HUD's short-lived Office of Neighborhood Development. The Comprehensive Employment and Training Act, which through its contracts and publicly funded job slots had supported many CDC staffs and organizers, gives way to a scaled down Jobs Training Partnership Act, to support training only. Subsidies for low income housing production are decimated. Urban Development Action Grants, are shrunken, so are budgets for the Economic Development Administration and numerous antipoverty programs. CDCs scurry to form new partnerships with private business, local government, and local and national foundations."<sup>2</sup>

With these changes many CDCs altered their structure, goals and objectives. They have become leaner in structure and modified goals so that they are more project than service oriented. CDCs receive financing from diverse private sector enterprises, including foundations and banks.

Banks have not only worked with CDCs, but some banks embrace the CDC concept as a useful mechanism for their own involvement and have begun to initiate bank CDCs.

### **BANK CDCs**

The term "bank CDC" is used as a generic term to describe bank sponsored CDCs, bank holding company CDCs, and bank investment corporations. Bank CDCs can be defined as subsidiary corporations established by banks "that address housing, small business, industrial and other needs in poorer communities. Such corporations can make use of powers otherwise prohibited to bankers such as buying, selling and managing real estate, taking equity positions in small businesses, acting as joint venture partners and dealing in syndications."<sup>3</sup>

The bank CDCs are created under powers granted by the Federal Reserve Board (FRB) and the Office of the Comptroller (OCC) of the Currency. State and local banking commissions and the

Federal Home Loan Bank also have regulatory power over bank CDCs. The OCC and the FRB regulations are highlighted in the next chapter, as they are the principal agencies regulating bank CDCs.

### **WHY STUDY BANK COMMUNITY DEVELOPMENT CORPORATIONS?**

In recent years community and economic development issues have become the focus of an increasing number of banks. Bankers realize that an important component of survival and profitability is their link to the economic well being of the community they serve. A bank's link to the community goes beyond merely receiving deposits and providing customer account services. Banks can also play a key role in maintaining stable communities by providing small business and residential loans. One mode which an increasing number of banks have used to help maintain stable communities and neighborhoods is a bank sponsored community development corporation (CDC).

Banks, local governments, and communities should investigate the potential of bank CDCs for several reasons. First, if bank CDCs are effective performers and valuable to community revitalization efforts, banks may want to expand their use and support of them.

Second, bank CDCs allow banks to make direct equity investments in community projects. In the absence of traditional CDCs, bank CDCs may serve as the catalyst for community development.

Third, if banks are operating in declining areas, with a concentration of low-income residents in dilapidated housing and a weakening commercial center, the bank's deposit base suffers. However, through bank CDCs, banks at least have one avenue of asserting some control over the decline. In some instances, bank CDCs may even substantially help reverse the decline.

Finally, a need for more information on bank CDCs still exists. Little has been written on the progress or potential of bank CDCs. Nor has there been much analysis of how the banks, the community, or the bank CDCs themselves contribute to community revitalization efforts.

Banks often find it difficult to provide loans for and make investments in low-and moderate-income communities. A great many urban neighborhoods and communities have been or are currently experiencing some form of decline. In some instances, economic shifts have led to the economic decline of cities. Major factories and industries close or relocate and inevitably public resources are shifted out of those areas as well. Public infrastructure begins to deteriorate and other public services such as fire and police are often cut back. Consequently, this type of disinvestment can lead to community destabilization and decline.

Banks traditionally do not perceive investment potential in such areas and are reluctant to lend to individuals who reside there. Investments in declining areas are not seen as being consistent with bank profitability. Beyond banks and bankers being averse to lending in declining areas, there still exist their reluctance to lend in communities with a large proportion of minorities. Unfortunately, minorities, usually black and Hispanic, comprise a large segment of urban communities' populations.

"Financial institutions do not appear familiar with inner-city neighborhoods," says Dr. Anne Schlay, a research scientist at Johns Hopkins Institute for Policy Studies "They don't know those neighborhoods. People come to what they know. A good investment is what they feel is secure and it's possible that white, middle-income bankers don't feel secure about those neighborhoods."<sup>4</sup>

Bankers often view minority communities as being unduly risky for loans and investments. In the past, bankers "red lined" around these areas and purposely refrained from lending to those communities (this became known as the discriminatory practice of redlining).

In an effort to end this practice, the government enacted two pieces of legislation, the Home Mortgage Disclosure Act (HMDA) and the Community Reinvestment Act (CRA). These pieces of legislation were the result of a groundswell of community activism aimed at increasing neighborhood reinvestment on the part of the banks and fighting against redlining. The community's agitation and protest efforts paid off in 1975 when the HMDA was enacted.

The HMDA "used federal regulatory power to require private lenders to reveal by census tract the number and amount of mortgage loans made and savings deposits held."<sup>5</sup> Throughout the hearings, bankers, federal regulators, and government officials proclaimed their opposition to the bill. Many denied that redlining existing while others focussed on the economics of requiring banks to gather and disseminate the data.<sup>6</sup>

The provisions of the Community Reinvestment Act of 1977 were to remedy deviations in availability for home mortgages. "CRA empowered federal regulators to review the community lending policies of financial institutions, and consider public challenges to a lender's service record in meeting local credit needs when deciding upon applications for branches or mergers."<sup>7</sup>

Both of these acts were intended to discourage discriminatory lending patterns across communities based upon race. However, the past eleven years with both the HMDA and CRA in effect have not seen the elimination of urban disinvestment. Recent research has pointed out consistent patterns of disinvestment and redlining in urban communities such as Atlanta, Detroit, Baltimore and the District of Columbia. In her 1985 study of District lending patterns, Dr. Schlay

discovered that banks have been investing far less in the District's minority communities than in white communities. Even accounting for an applicant's income and neighborhood housing stock conditions, the findings consistently point to race as the primary factor in determining who receives residential loans.<sup>8</sup>

The dispersal of capital to communities for development is even more crucial in view of the cutbacks and reductions in federal and local funding commitments for community economic development. Federal funding for housing programs has been reduced by more than 70% since 1981. More and more, community and neighborhood development organizations are looking to the private sector for administrative and project capital.

Banks in particular are receiving close scrutiny in light of recent findings regarding their selective lending patterns to communities. Some banks have developed a number of innovative ways to increase the amount of capital and credit flowing to their communities. Bankers have instituted special community development lending units for direct neighborhood lending. A growing number of banks are using CDC as their tool for enhancing local community economic development.

#### **QUESTIONS TO BE ADDRESSED AND METHODOLOGY**

This thesis seeks to increase our knowledge about bank CDCs and their potential usefulness in furthering community development efforts. It presents three case studies of bank CDCs,-- Black Business Investment Corporations, North Carolina National Bank CDC, and Chemical Community Development, Inc. to begin to address the following two questions:

- 1) What factors are critical to a bank CDCs organizational development and ability to achieve its goals? and
- 2) Based upon these critical factors, what criteria can be derived for assessing and strengthening the bank CDC model's influence on community and economic development?

Bank CDCs are incorporated for various reasons. Some banks form CDCs as a response to community protests. Community groups contend that they are not investing as much as they should in the community. Bank CDCs are also created to comply with the regulatory requirements of CRA. Still others are established for just one project and once that project has been completed the CDC becomes inactive. Others with an explicit interest in community economic development incorporate bank CDCs to make long term commitments and investments in the community.

The three case studies chosen represent the latter model of bank CDCs. The bank CDCs established with long term goals provide the greatest source of material for addressing the two proposed questions. These bank CDC models also illustrate a cross section of bank CDC structural types including a multi-bank investment corporation for entrepreneurs, a CDC focused solely on providing affordable housing for low and moderate income persons, and a CDC engaging in both commercial and neighborhood revitalization.

Assessment of the bank CDC models relies on significant primary research. Information on the three bank CDCs, as well as other CDCs mentioned, is derived from a blending of interviews of the CDC directors, public presentations by institutional representatives at forums and conferences, and published materials.

## **ORGANIZATION OF THESIS**

The introductory information presented in the first two chapters provides a framework for the appraisal of the forthcoming evidence relating to the thesis questions. Chapter three presents three bank CDC case studies. Each is analyzed in light of particular elements critical to the bank

CDC striving to achieve its goals and the obstacles which it may face. Chapter four discusses the overall implications of the findings in Chapter three. The chapter will conclude with recommendations and strategies for bank CDCs in the future.

1. Neil R. Pierce and Carol F. Steinbach, Corrective Capitalism: The Rise of America's Community Development Corporations. (New York: The Ford Foundation, 1987),p.27

2. Ibid. p. 29.

3. Martha R. Seger, "Opening Remarks," speech given at the Financial Institutions Community Development Corporations Forum. Office of the Comptroller of the Currency and the Board of Governors of the Federal Reserve System, Washington D.C. 13 August 1987.

4. Boston Globe, 1988

5. John T. Metzger and Marc Weiss, The Role of Private Lending in Neighborhood Development: The Chicago Experience. (Chicago, Illinois: Center for Urban Affairs and Policy Research, Northwestern University) March 1988, p. 18.

6. Ibid.

7. Ibid. p.20.

8. Boston Globe, op.cit., p. A46.

## Chapter 2 THE CONTEXT OF BANK CDCs

The purpose of this chapter is to set the context for further analysis of bank CDCs in chapters three and four. Each section attempts to encapsulate the basic elements which shape the bank CDC model and its environment.

### **RATIONALE FOR A BANK CDC**

The establishment of bank CDCs can help bankers achieve several goals at once. Banks improve upon their Community Reinvestment Act (CRA) record. A bank's CRA record is assessed on the basis of twelve factors to evaluate the bank's efforts at meeting local community credit needs.

The formation of a bank CDC allows banks to satisfy at least four of these criteria:

- o activities to ascertain community credit needs;
- o geographic distribution of credit extensions, applications, and denials;
- o participation in local community development and redevelopment projects
- o origination of residential mortgage loans, housing rehabilitation loans, home improvement loans, and small business loans.

One of the first duties a bank undertake before organizing a CDC is to define its initial task as completely as possible. This is usually a description of its first project area and community need to be addressed by the CDC, typically either housing or economic development. Included is the identification of a target group, program, or geographic area and the specific needs to be addressed. The community credit assessment acts as a marketing study to ensure that the bank has an awareness of the community's diverse credit needs.

The conventional wisdom of banks has been to lend in designated areas and ignore other areas perceived as being unduly risky. Ostensibly, bank CDCs direct and target resources for community development in low and moderate income communities. Bank CDCs thereby ensure that credit and capital are spread to areas often neglected. By extending its resources, the bank is not only allowing low income communities equal access but they also satisfy another CRA requirement.

Bank CDCs often initiate community development efforts in the absence of active community based development organizations. This endeavor makes them automatic participants in community redevelopment efforts. In addition, bank CDC's are routinely involved in making direct investments in low- and- moderate income residential development and small business development.

These endeavors satisfy two more CRA requirements. Bank CDCs can begin by targeting specific neighborhoods and communities. Their involvement often supports and encourages other private sector investment in community development efforts. Depending on the CDC's activity --housing or economic development-- cumulative project effects ( ie., job creation and/or rehabilitated or newly constructed housing) may serve to increase a bank's future lending and depositor base.

Based upon their activities, bank CDCs can also direct community development in specific areas. This is often done to spur the revitalization of one area with the hopes it will interest other developers and have a spill over effect into the revitalization of other areas. However, a bank's role in actually leading and directing community development effort is a sensitive one.

Creation of a CDC allows the bank to centralize community development financing expertise in one identifiable unit. This gives the community by a one-stop unit which can handle their various needs. It benefits the bank by having one unit which can coordinate community development activities.

One of the most influential factors in determining why a bank CDC is established is bankers' attitudes and philosophy towards community lending and investment in general. A great many bank CDCs received their start as a result of an aggressive Chief Executive Officer or community lending officer. By choosing to use the CDC, the bankers gain a vehicle to expand the bank's community involvement through equity investments in projects. Banks can significantly alter their reputation in the community by creating a CDC. A bank CDC can move the bank into a leadership role which gains the public's attention, respect and cooperation.

For the community, one of the benefits bank CDCs can provide is the expertise and capital for development projects. Also community advisory committees, "ensure a forum for community input where such input might otherwise be absent."<sup>1</sup> Even with community input there might be a lack of community control if the committees are not a true voice for the community and some merely as rubber stamps for the CDCs policies.

## **RISKS**

The risks that bank CDCs can pose for banks include constraining the bank to a long term leadership role in community development. If this happens, the bank must assume the responsibilities of this commitment. Bank CDCs may also tend to limit the scope of the bank's investment in other project or program areas.

Bank CDC may face numerous community relations problems if the target area rejects the CDC, if other areas question the CDCs method of targeting areas, or if existing CDCs see it as unnecessary.

There is the risk that management will be not be supportive of the CDC. Also, setting up

another unit can be costly for the bank if it must allocate additional funds for staff as well as projects.

Two notable risks faced by the community are a reduction in overall credit and negative project impacts. The community may suffer if the bank decides that CDC activities are sufficient and other credit and lending programs are reduced. Negative project impacts may also be a risk to the community if, for example, the project causes displacement of residents.

### **COMPARISON OF BANK CDCs AND TRADITIONAL CDCs**

Bank CDCs are intended to stimulate and support community development, not compete with traditional CDCs. Their existence in geographic and project areas is often more appropriate when: 1) a financial gap exists that cannot be met by existing public and private organizations; 2) an initial capital injection for a project is required to facilitate the participation of others; 3) a new organizational framework is needed to stimulate action on community needs.<sup>2</sup>

Bank CDCs, with the support their parent company, take on many of the same primary activities as traditional CDCs, such as housing or economic development. Like traditional CDCs, bank CDCs do not all perform the same tasks although a majority of them are involved in an aspect of housing development. Bank CDCs and traditional CDCs can both be structured as nonprofit or profit community development organizations. They both form partnerships with local governments and other investors which serve to broaden their base of financial and community support.

However, there are a few notable differences between traditional CDCs and bank CDCs. One of the primary differences is the capitalization of bank CDCs versus traditional CDCs. Bank CDCs, unlike traditional CDCs, are not as concerned about raising operating or project funds.

Bank CDCs have the initial and continuous financial support of their parent bank (s). On the other hand, traditional CDCs can be multipurpose organizations, sometimes even active in human services and advocacy activities. Bank CDCs are primarily project oriented but will provide services as part of their comprehensive community development activities.

One of the most important differences is that traditional CDCs are set up to empower communities therefore they have a built in support constituency. Bank CDCs are not necessarily set up to empower communities, have very limited avenues for community input, and may have to prove themselves to the community in order to build a supportive constituency.

## **BANK CDC REGULATIONS**

There are a variety of regulations governing bank CDCs. Bank CDCs initiated by a national banks are regulated by the OCC. Bank holding companies (BHC) CDCs are regulated by the Federal Reserve Bank. Nearly, sixty bank CDCs are regulated by both the OCC and the Federal Reserve Bank. Because some banks have multiple investors, including national investors, there is some overlap among the two regulators. The Federal Home Loan Bank Board regulates bank service corporations for federal savings and loans and state banks are regulated by state. State Bank commissions also implement regulations which govern bank CDCs. Because they are the foremost regulating agencies of bank CDCs, this section will focus only on the regulations of the OCC and the Federal Reserve Board.

### **Office of the Comptroller of the Currency: National Banks**

The Office of the Comptroller of the Currency (OCC) regulates national banks and their establishment of bank CDCs. The OCC's Interpretive Ruling (see Appendix A for full citation), issued in 1978, permits national banks to create or invest in CDCs. The banks can participate in CDC ventures through various mechanisms under the OCC program including: 1) establishing

wholly owned bank subsidiary CDCs; 2) assisting in the formation and capitalization of multi-bank CDCs; and 3) investing in qualified community development ventures or projects. These investments are normally not allowed for national banks under OCC regulations. However, the OCC allows bank investments in CDCs or other community development projects in order to stimulate community growth, to fill an existing financial void which cannot be met by public or private organizations, or to act as a catalyst in encouraging outside investment sources to participate.

The application process under the OCC's program requires that national banks interested in establishing CDCs prepare and submit an investment proposal to the OCC. The proposal describes the purpose of the CDC including how it meets the public purpose stipulation in OCC's rules; a description of incorporation as for profit or nonprofit; the board of directors, advisory committees and community involvement; the nature of the bank investment; the CDCs target operational areas and beneficiaries; projects; staffing arrangements; and an implementation timetable. The OCC then reviews the application for compliance with the requirements of bank CDC incorporation and current banking laws. For purposes of expedition, draft proposals may be submitted to the OCC in advance to insure that proposals will meet OCC guidelines. In some cases, the OCC will also request site visits to the CDC project area, meet with the banking establishment, or confer with other interested or relevant parties including community groups.

The OCC then issues an opinion letter to the bank stating whether the proposal is permissible for the bank and legal under Interpretive Ruling 7.7480. The opinion letter generally takes 60 days from the OCC's receipt of the final formal investment proposal.

Proposals are evaluated by the OCC on a case-by-case basis in order to account for a wide range of activities undertaken by CDCs. In determining whether the CDC serves a predominately

public purpose, the OCC considers the following:

- o Will the CDC benefit low and moderate income areas, residents, and small businesses?
- o Will the CDCs program address agreed upon community goals and needs?
- o Will the CDC fill an existing gap not addressed by the private sector?

The OCC measures program aims such as economic development, commercial revitalization, or housing against more specific guidelines relative to the local community needs. For example, in a proposed CDC housing rehabilitation program, the OCC would assess the possible displacement impacts housing renovation might have upon project implementation and completion.

Project staff is also assessed by the OCC. Bank CDCs have an advantage because they provide required expertise in specialized areas such as housing or real estate. The proficiency of bank CDC staff in such fields serves to expand the types of activities the CDCs may undertake as well as increases the chances of project success.

The costs pertinent to bank CDCs can be shared among several banks. The OCC has no restrictions on the number of banks forming or investing in CDCs as long as the banks meet the public purpose guidelines set forth by the OCC. OCC rules also stipulate that total funding for bank CDCs cannot exceed 5% of the bank's surplus and capital nor can one project investment exceed 2% of the bank's surplus and capital.

Within six months of incorporation, OCC regulations require CDCs to submit a detailed plan for the first and second years of operation. Annual reports which summarize activities and activity progress must be submitted as well. Bank CDCs are authorized by the OCC to acquire, construct, manage, sell and/or promote real estate in targeted communities; loan, grant and make equity investments to promote projects related to the CDCs activities; provide of technical

assistance in planning, finance and implement related activities; serve as a clearinghouse of information between the bank and the community; and conduct community related studies.

#### **Federal Reserve Board: Bank Holding Company**

The FRB regulations for bank holding company (BHC) CDCs are not as comprehensive as those promoted by the OCC. Consequently, they are somewhat less restrictive than OCC regulations. In 1970, amendments to the FRB's Bank Holding Company Act [12 CFR 225.4 (a) (7)](See Appendix B for full citation), authorized banks to engage in "permissible nonbanking activity, equity and debt investments by bank holding companies in corporations or projects designed primarily to promote community welfare, such as the economic rehabilitation and development of low-income areas."<sup>3</sup>

This amendment was added after the FRB had witnessed the success of the first CDCs and "felt that bank holding companies could and should help in this effort since their banks are a known, trusted and legitimate community institution."<sup>4</sup> The Board felt their position as a legitimate institution would enable them to act as a liaison linking the community with other private and public resources thus encouraging greater public-private partnerships. Thus, changes in the banking laws were partially created by a growing realization on the part of banks that they could do more to partner with local governments and communities to promote community development.

A 1972 amendment refined the earlier definition to specifically state that while the Interpretation "primarily focuses on low-and moderate income housing, it is not intended to limit projects ... to that area."<sup>5</sup> This amendment further set standards by which BHC CDC proposals are evaluated in relation to meeting a public benefits test. This test clearly states that the community must be the primary beneficiary of all activities.

More importantly, the BHCs investment must be critical to the project. Specifically, if there was no participation on the part of the BHC and the project could not get done, this would meet the public benefits standard and be an allowable investment.

The Federal Reserve allows BHC CDCs a great deal of flexibility in determining the level of investment the holding company may make in the CDC. Unlike the OCC's 2%/5% rules, there are no stated minimum or maximum levels of CDC or project capitalization. The Federal Reserve does review the level of bank commitment regarding staffing and capitalization but has no criterion by which to gauge adequate funding or staffing levels.

BHC CDCs are not geographically limited and may operate in any neighborhood. Consequently, BHC CDCs are not necessarily set up to benefit low and moderate income areas and residents. The governing regulations for BHC CDCs do not require community involvement on the board of directors. This apparent lack of community participation can limit the BHC CDCs ability to accurately reflect community objectives and perspectives in determining the CDCs priorities, plans, and projects. Accordingly, the Board's public benefit standard explains demonstration of a public purpose was enough to warrant a permissible bank investment.

Applications to form BHC CDCs are submitted to the Federal Reserve Board along with a memorandum stating how the proposed CDC project will meet the community development objectives in line with 1972 interpretation. Specifically, the FRB considers the following:

- o Whether the CDC is for a single or ongoing project?
- o What the maximum investment will be in the CDC and what are future income projections?
- o What other parties will be supporting the project and in what capacity, either technical or financial?
- o What is the target group and geographic area?

- o Who will be managing the day-to-day operations, what are their qualifications?
- o Are there any questionable aspects of the CDC which need to be explained after the Board has completed a project review?

Applications for CDCs are handled within thirty days of processing by the local Reserve Bank unless there are questions related to its creation which must be reviewed. Once the CDC is established the Board does not require any special reporting on its activity. But the CDC is reviewed annually at the same time as the holding company.

### **BANK CDC MODELS**

Bank CDCs engage in activities which their parent banks are not normally able to undertake. By utilizing the original capitalization provided by the parent corporation as well as leveraging project and capitalization funds, a bank CDC can: act as real estate developers for residential, commercial, mixed use and/or industrial projects; act as lenders to make loans and projects feasible under the banks underwriting criteria ; act as seed capital investors for minority/small business development; and undertake public work projects. Based upon their activities, bank CDCs, can be categorized into six models:

- 1) Housing Real Estate, rehab and/or construction;
- 2) Commercial Revitalization;
- 3) Housing/Commercial Revitalization;
- 4) Business Development; and
- 5) Multiple Activities;
- 6) Lending and investing units.

Bank CDCs activities may also include technical assistance to community groups, market research,

promotional campaigns, and a variety of public service projects.<sup>6</sup> Regardless of the CDC project, it must demonstrate public purpose benefits.

### **Housing Real Estate**

The most common activity for bank CDCs to undertake is housing rehabilitation. Very few are involved in actual new housing construction. A number of bank CDCs are involved in "buy-rehab-sell" housing development. They are able to rehabilitate units quickly, sell them (often to tenants) and reinvest the sales proceeds into other projects.

Indiana National Neighborhood Revitalization Corporation (INNRC), a for-profit bank CDC of Indiana National Corporation, adopted the buy-rehab-sell approach to increasing the affordable housing stock in the Indianapolis area. Specifically, INNRC confined its initial rehabilitation efforts to three strategically chosen low - and moderate -income neighborhoods because they have strong neighborhood associations. The neighborhood associations determined the most needy areas within their communities. INNRC purchased and rehabilitated three or four of the blighted and deteriorated single-family homes for sale to low - and moderate -income persons. The CDC made every effort to avoid neighborhood displacement by providing counseling and referral of low -and- moderate income persons to bank branches for mortgage credit to purchase the renovated homes. Subsidies required to make units affordable were contributed by the government programs.<sup>7</sup>

First Fidelity CDC has not been able to meet corporate goals with their buy-rehab-sell endeavors. The New Jersey based First Fidelity CDC undertook rehabilitation activities of two units on its own and lost money. Subsequent efforts to develop 6 modular units also did not meet corporate expectations and eventually led to the decision not to act as housing developer."<sup>8</sup>

What differentiates INNRC experience from First Fidelity's is that in the former case, the

CDC had community input in terms of determining the communities housing needs and priorities. INNRC also provides neighborhood services and financial counseling. "First Fidelity CDC ..., lacked community contact and development experiences."<sup>9</sup>

### **Commercial Revitalization**

Bank CDCs also emphasize commercial and downtown revitalization activities. As part of larger economic development projects, Norwalk CDC of Norwalk, Ohio, and Seagate Community Development in Toledo, Ohio have done commercial projects. Seagate, before its reorganization and subsequent inactivity, was a major actor in helping to complete Toledo's waterfront and downtown revitalization plans. Norwalk CDC was incorporated for the purpose of both restoring downtown properties and increasing jobs. First Fayetteville CDC had attempted commercial revitalization activities during the early 1980s. However, due to two changes in bank ownership over a five year period, CDC activities were not given high priority and only one rehabilitation project was completed. Since that time, downtown revitalization has occurred without CDC efforts although the CDC did serve as the catalyst to bringing the business and banking community together."<sup>10</sup>

### **Housing and Commercial Revitalization**

North Carolina National Bank CDC is a primary developer in both housing and downtown revitalization activities in the Raleigh and Charlotte, North Carolina areas. NCNB's CDC activities are explored more fully in the Chapter 3.

### **Business Development**

The Southeast Bank in Miami has undertaken a unique bank CDC vehicle for minority business development and job creation. The Business Assistance Consortium CDC (BAC CDC), established by a number of banks in the Miami area, provides venture capital for black-owned

and operated firms in Dade County, Florida. The BAC CDC's activities are explored more fully in Chapter 3.

### **Multiple Activities**

Bank CDCs have chosen to be involved in a number of different types of projects. Employing a more comprehensive approach allows bank CDCs to have a greater impact on the community. Shorebank is the most comprehensive example of a bank CDC undertaking multiple activities. It has two parallel CDC which function in a variety of activities including housing rehabilitation, technical assistance to community groups, employment training and placement, and the promotion of housing cooperatives.<sup>11</sup>

### **Lending and Investment Units**

A growing number of bank CDCs are established as lending vehicles. This type of CDC provides a link to the community by funding traditional CDCs and other community groups for a variety of programs. Chemical Community Development, Inc. is an example of a CDC which provides recoverable grants, which are really loans, for nonprofits to pay their initial construction costs. Typically, loans are granted at favorable terms with flexible repayment. However, the Black Business Investment Corporations of Florida are set up to provide gap financing for businesses and offer rates and terms similar to a banks.

Bank CDCs also provide the equity and debt for projects and joint ventures which might not otherwise be feasible projects. The structure of deals where the CDC is providing debt financing are often complicated by the inflexibility of the banks underwriting criteria. Generally, banks will not alter underwriting criteria, however they are willing to take a subordinate position behind other lenders. Mellon Bank CDC has been willing to take a secondary position or defer principal or interest on loans in order to make small business projects and loan mortgages bankable.<sup>12</sup>

By and large, bank CDC projects require multiple sources of debt financing including city or other private sector investors. Loans made by bank CDCs are more complicated than loans made through traditional lending institutions. Multiple financing sources are not uncommon and the nature of government loan programs is such that their turnaround time is usually delayed. Community economic development loans require greater flexibility, coordination, and technical assistance to package the projects.

Equity financing for projects can be more flexible. First Bank System CDC of Minnesota, a for-profit CDC, participates only in joint ventures with nonprofit partners. They fashion partnership arrangements in a variety of ways: 1) act as general partner/owner, with the nonprofit as the lessee; 2) act as co-general partner with the nonprofit; 3) act as a limited partner and the nonprofit as the general partner.<sup>13</sup> Providing project equity financing is less complicated than project debt. There are no limits on the amount of equity which may be invested to make projects viable.

### **BANK CDC STRUCTURE**

Bank CDCs can be incorporated as profit or nonprofit entities. The way in which CDCs are structured determines its eligibility for resources and its use of revenue. This section provides a discussion of the advantages and disadvantages of profit and nonprofit bank CDCs.

Bank CDCs that are established by a number of financial institutions, often referred to as a multi-bank or consortium CDC. Multi-bank CDCs may be for profit or non-profit. Bank CDCs can also be organized as multiple entities utilizing both for and nonprofit CDCs to carry out community development projects.

## **Nonprofit CDC**

Nonprofit bank CDCs are eligible for foundation endowments and special government assistance programs such as the Small Business Administration guaranteed loans. A nonprofit bank CDC structure is also very appealing to potential donors because of the tax shelter and benefits possibilities. In some states, private organizations making contributions to nonprofit groups participating in community development are eligible for 50 percent state tax credits. In addition, depending on how projects are structured, nonprofit CDCs can act as intermediaries in facilitating the cash-flow benefits to other private investors. Moreover, because of the nonprofit tax exempt status, any surplus in funds can be reinvested back into community development projects. Excess income earned by bank CDCs can also be funneled to the sponsoring bank and used to leverage its initial capitalization. Generally, because they are not seen as potential profit makers and therefore future competition, nonprofit bank CDCs are perceived to be more politically acceptable to the local government, area developers, and the community.<sup>14</sup>

One example of banks wishing to maintain the goodwill of the community was explained by Frank Kohne, former President of the now inactive Mellon Bank CDC (MBCDC). Mr. Kohne stated that because many of community based development organizations and the for-profit housing developers banked with Mellon Bank, MBCDC was formed as a nonprofit so as not to be perceived as competition for the customers.<sup>15</sup>

Finally, it is often difficult for "profit" motivated bankers to relate to "nonprofit" bank created entities. Bankers view such entities as social give away programs with no return to the bank. This can create operational difficulties for the CDC if management does not quite understand the initial function of the bank CDC and hampers its growth and community development efforts.

### **For-Profit CDC**

Bank CDCs established as for-profit entities offer a number of advantages for banks and potentially for the community. In general, the majority of bank CDCs are formed as profit entities for various reasons.

First, for profit CDCs helps to attract additional funding from outside sources who need tax-shelter benefits. Additionally, under the 1986 tax reform bill, for-profit CDCs developing low income housing may utilize the low-income housing tax credits offered. Under the tax reform bill, private investors are granted tax credits for investing in the development of low income housing. By providing such tax advantages, the CDC is not only benefitting the bank and investors, but the community which gains additional reinvestment as a result.

Like many other profit organizations, this structure of bank CDC is able to sell organizational stock in order to increase its base of funds. For-profit bank CDCs can also generate fee-income by providing technical and consulting services to for-profit and non-profit developers and local government.

Banks may also elect to incorporate as for-profit to stress the value and potential profitability of community development projects. Bank CDCs projects that do well can be profitable and yield a return on equity. In turn, this means a real impact on the parent bank's overall economic performance.

A for-profit CDC is structured much like any business set up to make a profit. This can be appealing to bankers who have a thorough understanding of for-profit corporations. The corporate mentality of bankers often dictates that the CDC show a specified bottom-line profit in order to

be deemed successful. Initial support for a bank CDC can be contingent on the amount of profits realized from community development projects.

One significant disadvantage of for-profit CDCs is that they are ineligible for special government programs such as Small Business Administration (SBA) guaranteed loans. However, the CDC can make equity investments in projects and the parent bank can then participate in the government sponsored loan programs for housing or economic development. For-profit bank CDCs are also disqualified from accepting charitable donations and grants. For-profit CDCs are also subject to state and local corporate tax regulations.

Issues of "turf" may arise if other CDCs are operating in the same geographic and project areas. Being seen as a competitor for projects can be an obstacle to the bank CDCs ability to influence community economic development. For these reasons, bank CDCs are viewed skeptically by the community, for-profit CDCs are viewed with far more distrust than nonprofit CDCs and may meet with greater community opposition.

#### **Multi-bank or Consortium CDCs**

The establishment of bank CDCs is not limited to one bank; many bank investors may come together and form a consortium in order to sponsor a CDC. The CDC can be either for profit or nonprofit. The multi-bank CDC is one way the local banking community can collectively address the specific needs of the community.

Typically, an aggressive lead bank, with an awareness of community credit needs, is responsible for encouraging other banks to participate in a consortium. A good example of this type of bank is the Southeast Bank of Miami, Florida. In 1982, the Southeast Bank approached the OCC with the concept of establishing a multi-bank CDC. The bank had already established a small, minority business technical assistance program but felt all the banks in Dade County should

join forces to ensure increased access to local non-minority markets for minorities. Through their efforts at enlisting other banks, there are currently 25 banks which offer assistance programs geared specifically at the black business community. The structure and endeavors of the Business Assistance Consortium CDC, part of the Black Business Investment Corporation network, will be described in greater detail in chapter three.

Participating consortium banks share the risk and costs which they often feel are associated with community development activities. The multi-bank CDC structure is also a useful vehicle for those banks wishing to invest yet not acquainted with local community credit needs. Banks working together under a consortium structure can coordinate and direct community development efforts rather than have several banks engaging in small scale, low impact projects or duplicating efforts.

A notable disadvantage consortium banks have is the potential for disagreement on project investments. A good example is illustrated by a multi-bank CDC incorporated in New Jersey. Four banks, led by First Jersey Bank, formed a multi-bank entity designated Evergreen CDC in New Jersey. Constant disagreement regarding which projects to undertake and bankers' refusal to commit financing to projects consequently led to the abandonment of several community development activities. Currently, First Jersey is the sole investor in Evergreen CDC.<sup>16</sup>

Moreover, banks often see consortiums as being an ideal way of satisfying CRA requirements with a nominal investment. Once they have made an investment, they may do little else for community development nor are they particularly active in the CDC's activities.

#### **For Profit CDC and Nonprofit CDC Affiliate**

Another method banks can use to structure CDCs is through organizing a for-profit CDC and

a non-profit CDC to operate simultaneously. This model of a bank CDC is best exhibited by the Shorebank Corporation, a bank holding company which has two for-profit CDCs and one nonprofit CDC.

In the Shorebank Corporation, its for profit CDC, City Lands Corporation, acts as a real estate company which develops and manages residential and commercial property for low-and moderate-income residents. Its non-profit affiliate, The Neighborhood Institute (TNI), provides job training, small business development and housing rehabilitation for the residences managed by City Lands. A for-profit subsidiary of the Neighborhood Institute, the TNI Development Corporation, was formed to develop low-income housing using the 1986 tax reforms aimed at providing incentives for private investors to invest in low income housing.<sup>17</sup>

However, while multiple entities allow for maximum funding possibilities, greater flexibility and potentially beneficial tax considerations, they require increased staff and complex capitalization requirements depending on the number and type of bank involved in the consortia.

1. Brett M. Doney and Bridget K. Nedzi. "Bank Sponsored Community Development Corporations: A Private Sector Initiative for Community Development." Paper presented for MIT course 11.947,11 May 1983, p.23.
2. Roundtable Sponsored by the Office of the Comptroller of the Currency. Opportunities and Issues for Banks in Affordable Housing. (Washington, DC., 1986), p. 46.
3. Community Development Division, Office of the Comptroller of the Currency, Program Guidebook to Help Meet Community Credit Needs: A Guidebook for Banks and Bank Examiners (Comptroller of the Currency, Administrator of National Banks, Washington, DC, September 1979), p. 35.
4. Federal Reserve Board, "CDC Bulletin Article," draft of an internal memorandum, not dated.
5. "CDC Questions and Answers," (Federal Reserve Board, Washington DC, November 1983) p. 3.
6. Doney and Nedzi, op cit., p. 17.
7. Office of Comptroller of Currency and Board of Governors of the Federal Reserve System, Financial Institutions Community Development Corporations Forum (Washington, DC, 1987), pp. 9,50.
8. Alma Balonon, "Bank Sponsored CDC Paper," (inter-office memorandum submitted to The Ford Foundation New York, August 1988), p. 13.
9. Ibid.
10. Ibid.
11. Ibid p.20.
12. Office of Comptroller Currency and Board of Governors of Federal Reserve Board, op. cit., p.14.
13. Ibid p. 26.

14. Doney and Nedzi, op. cit., p.12.

15. Ibid p.12.

16. Balanon, op. cit., p.10.

17. Office of Comptroller of Currency and Board of Govenors of the Federal Reserve System, op. cit., pg.15.

## Preface to Case Studies

Bank CDCs are characterized by a high degree of flexibility that enables the parent bank to tailor a CDC to the communities particular needs. This flexibility makes a operating bank CDC difficult to describe in generic terms. <sup>1</sup> The common element shared by bank CDCs is the activities they undertake are expected to directly benefit low-and moderate-income groups.

The priority of needs vary from one community to the next. Often the priority and order in which they get addressed depends upon who is defining the need. Community groups can strongly recommend an area in which banks should direct community development efforts. Banks can also develop their own strategy and concentrate CDC efforts in project areas where they have some degree of expertise or in targeted geographic areas receiving additional public investment.

The purpose of this chapter is to analyze in greater detail the origin, type, and various activities of three CDCs to illustrate how techniques/strategies have been used to enhance bank CDC activities. Specifically, this chapter will attempt to answer the first question posited in chapter one: What factors are critical to a bank CDCs organizational development and ability to achieve its goals.

The CDCs chosen for analysis represent diversity in bank size, bank involvement, CDC structure, and geographic areas. The Black Business Investment Corporations (BBICs) of Florida focus on minority business and economic development. The North Carolina National Bank (NCNB) CDC addresses both economic development and housing issues in blighted communities and Chemical Bank Development, Inc. concentrates on lending for affordable housing and real estate.



Chapter 3  
**BLACK BUSINESS INVESTMENT CORPORATIONS (BBICs):  
Minority Business and Economic Development**

Often out of significant events the impetus for change arises. The 1980 riots in the Miami area were the catalyst for the creation of the Black Business Investment Corporations (BBICs) of Florida. These corporations were created by the Black Business Investment Board (BBIB) of Florida to revitalize and strengthen communities by providing capital to entrepreneurs. Specifically, the BBICs provide resource and technical assistance to black businesses who have traditionally lacked access to capital.

**TYPE OF BANK CDC**

The Black Business Investment Corporations (BBICs) are examples of innovative multi-bank consortia sponsoring a network of investment corporations. Each BBIC has a minimum of four banks as sponsors. The BBICs, six independent, nonprofit organizations, each with their own executive director, were created to provide capital to black business enterprises in Florida. The BBICs are governed by the BBIB which guides their overall operations. The BBICs are regulated by both the OCC and the FRB because of the types lending entities which have invested in them. The various investment corporations are located throughout Florida in Jacksonville, Orlando, Tampa, West Palm Beach, Miami, and Fort Lauderdale.

**ORIGIN**

In a speech given by Newell Daugherty, executive director of the Business Assistance Consortium CDC, a BBIC in Miami, he recalled how the consortium evolved. He related how in 1980, the anger and frustration of the black community in the city of Miami and Dade County produced one of the most deadly riots in the country. At the time, a strong, influential Hispanic business community and a dominating white business community existed; but neither group included blacks in their economic growth or in the job market. The 400,000 blacks in Dade

County had almost no involvement in the business community and had extremely high unemployment.

As a result of the riot, the business community joined forces and raised \$6.9 million to develop black businesses in Dade County. The Business Assistance Center (BAC) was created in 1982 to serve as a one-stop technical assistance center serving established and new black entrepreneurs.<sup>1</sup>

Southeast Bank, N.A., an aggressive area bank lender and investor, invested in the BAC and encouraged other banks to participate. Led by Southeast Bank, a group of banks interested in taking part in the BAC's activities approached the OCC for permission to organize the first multi-bank consortium CDC. The OCC granted permission and the Business Assistance Consortium CDC began in 1983. The Southeast Bank, believing that all the banks in Dade County should be committed to community economic development, obtained further commitments and raised an additional \$1.6 million from the other local banks and now has a 25 bank consortium. They strongly supported the passage of the 1987 Small and Minority Business Assistance Act.

The Small and Minority Business Assistance Act represented the State's recognition of the growing disparity in the economic and social well-being of black business and trades people in Florida.<sup>2</sup> For the black business community, recognition of their need for greater access to capital was finally acknowledged and beginning to be accommodated.

The Small and Minority Business Assistance Act created "several new entities within state government to address the needs of small and minority businesses, and altered various state procedures with regard to procurement, enforcement, and legislative reporting of state agency transactions with black businesses."<sup>3</sup> The Small and Minority Business Assistance Act created a 15 member advisory group to monitor the implementation of the legislation and provide a

forum for hearing the needs of small and minority businesspersons. The legislation also created the Minority Business Enterprise Office to assist minority businesses in contract procurement. Additionally, the Small and Minority Business Assistance Act established the Black Business Investment Board.

Florida instituted a \$5,000,000 Investment Incentive Trust Fund to be administered by the Florida Black Business Investment Board. The Florida Black Business Investment Board is a seven member board of trustees appointed by the Governor. The legislative mandate to the Board is to use the resources of the Fund in the creation of programs fostering development and expansion of black business enterprises. <sup>4</sup>

## **FUNDING**

To accomplish this broad legislative mandate, the Board invested in CDCs which raised initial capital of \$500,000 and provided matching state funds. It also established the Black Business Investment Corporations which were modeled after the Business Assistance Consortium CDC.

The BBICs, including the Business Assistance Consortium CDC, are the mechanisms by which the Board has been able to develop business assistance networks, entrepreneurial development programs, and provide a multitude of other capital instruments meant to enhance black economic development.<sup>5</sup> The funding base structure of the BBICs also includes the lending institutions, insurance companies, and other corporate contributions.

The number of bank investors varies in each BBIC. For example, the Palm Beach County BBIC, given approval in 1987, has four bank investors and the Black Assistance Consortium (BAC), approved in 1982, has twenty-five bank investors. The difference in bank investor number is partially attributable to the BBICs geographic location, the number of banks which service that

area, and the length of time it has been organized. Additionally, local governments grant administrative and operating funds to each BBIC.

This mixture of public and private funds to capitalize the BBICs and their activities has allowed each to expand its program capability and capacity. The BBICs are able to leverage these funds and thus increase their financial base and investment ability.

The primary goal of the BBICs is to foster and promote the growth of black businesses in Florida. The activities which they undertake reflect this goal. Inevitably BBICs focus on assisting businesses to create job opportunities which stimulate local economies. The BBICs utilize a number of techniques to achieve their goals and objectives.

The BBICs are authorized to provide a full range of financial assistance to businesses in the form of equity investments, loan guarantees, working and venture capital, and leveraged buy out and acquisition financing.

The newer BBICs have been in operation less than two years. They are still expanding programs and formulating additional programs such as the Black Contractors Cooperative. In its full operational stages, this program will assist businesspersons to: 1) purchase at bulk rate discount; 2) provide funding for bonding; 3) provide technical assistance for contractors; and 4) match prospective contractors with state agencies.<sup>6</sup> Besides this program, the Board has created a support corporation for the black businesses in Florida.

## **PROJECTS**

The Business Assistance Consortium CDC, organized for nine years, has the most comprehensive

programs for assisting black businesses. The scope of activities and programs administered by the Consortium give a clear picture of the potential growth and capabilities of the BBIC network.

The Business Assistance Consortium CDC operates not only under the umbrella of the BBIC but under the auspices of the Business Assistance Center. The Center's programs include education through its Entrepreneurial Institute, assistance in identifying market opportunities and customers, and a business incubator facility.<sup>7</sup>

The BAC's educational component, the Entrepreneurial Institute, conducts 12 week workshops which educate small businesspersons as to the components of business plans and their preparation. At the end of the course, participants are expected to be well acquainted with the intricacies of adequately planning for their businesses, both financially and managerially. Satisfactory demonstration of these skills is often critical to the success or lack thereof of start-up businesses during their first year of operation.

The Consortium also uses corporate volunteers as consultants to work individually with businesses. They are able to contribute knowledge and skills which the BAC could not otherwise afford. The Consortium is also beginning a pilot program to launch the BBIBs new Franchise Technical Assistance and Finance program. This program will provide the "black franchisee with items such as capital structuring of the franchise acquisition, negotiations with and between the franchisee and franchisor and financial analysis of the operation of the franchise for up to eighteen months after start-up".<sup>8</sup> Their goal is to complete 10 franchise deals. If the venture proves successful then the other BBICs will institute franchise programs next year.

## **PROJECT IMPACT**

As of January 1989, the total outstanding loans made since the BBICs inception were \$9.09

million. According to the BBICs 1988 annual report, the BBIC network disbursed \$2,009,700 of its funding to over 40 black businesses throughout the state creating 211 new jobs for the year.<sup>9</sup> In its first year of operation, the Tampa BBIC produced \$471,000 in loans or 20.7% of the total portfolio of BBICs. The Business Assistance Consortium CDC, which was not a start-up BBIC, generated 67% of the portfolio by September of 1988. The loans granted by the BBICs averaged approximately \$52,341 and created jobs at a cost less than \$13,765 per job.<sup>10</sup>

While the BAC provides the technical assistance required by black businesses, the BAC CDCs most important function is to make loans. Recently, the Consortium reported that in the first half of its 1989 fiscal year it had lent almost two thirds as much money as it did in all of 1988. In 1988, the Consortium had lent a total of \$1.6 million to fourteen applicants. This year it has already lent \$942,500 to nine applicants and expects to lend more.<sup>11</sup>

Participating banks' contributions have helped the BAC raise \$8.3 million since 1982. Since that time they have loaned \$10 million and made 75 loans. To date, approximately \$5 million has been repaid and another \$4.5 million is outstanding. Due to business failures, \$500,000 has been written off.<sup>12</sup>

An increase in the size of the loan has been one of the reasons for the increase. The Consortium made its largest loan, \$400,000, to an office supply company. The executive director, Newell Daugherty, expects that the CDC will continue to lend more in the next 18 months than its lent in its first five years.<sup>13</sup> Another reason for the optimism of the BACs executive director is the appointment of an aggressive new BAC Chairman. The new Chairman is intent on making even more loans at a quicker rate and is personally willing to provide any technical assistance necessary to accomplish this.

## **STAFF**

For the most part, BBIC staff size is relatively small, typically operating with only an executive director and administrative assistant. Because they are still in developmental stages, the executive director is responsible for the daily administration of the BBIC. This includes responding to loans requests, advising borrowers, preparing the proper loan documentation, and monitoring the loan once it has been disbursed. Once the BBICs have matured and increased their capabilities it is expected that they will increase their staff size to accommodate staff specialist to undertake selected aspects of the various programs.

## **THE BOARD OF DIRECTORS**

The governing board of each BBIC consists of bankers, community people, and public sector representatives. The BBIB has no veto power over loan decisions made by the BBICs but does ensure that the BBICs adhere to the law and the legislative intent of the Small and Minority Business Assistance Act. The BBIB monitors the quality of the lending portfolio to ensure the soundness of loans and develops other programs for the BBICs to administer. The board members vary in their degree of participation in guiding the BBICs operations. The individual BBICs may have a Board of Directors which participates in BBIC activities. The Chairman of the Board for the BAC plans to donate one day a week to provide assistance to BAC clients. The Loan and Investment Committee is comprised of seven persons, 4 bankers and 3 lay people. The Finance Committee has 4 persons, 2 bankers and 2 lay persons. A Community Advisory Committee of 7 is comprised of a majority of 4 lay people and 3 bankers.

## ANALYSIS AND COMMENT

The Black Business Investment Corporations are unique community investment corporations supported by lending institutions, insurance companies, and state and local government. While there are many special lending programs and even CDCs set up to provide technical and resource assistance to minority businesses, this network concept targeted specifically towards black entrepreneurs is the first of its kind in the country.

The BBICs have begun to receive increasing public support despite complaints from the black community about slow lending process. Part of the discontent with the BBICs is reflective of their businesslike approach to lending. As the executive director, Cleve Warren, explained, "the BBIC does not give away funds."<sup>14</sup> The quality of the deals have gotten better as businesses have come to understand the role and function of the BBICs. Their role is not to supplant lenders, but to provide the necessary financing between what the lenders offer and the borrowers requirement.

The BBICs have loan underwriting criteria based upon bank standards. However, unlike banks, the BBIC provides the technical as well as financial assistance often needed to make loans work.

Working with banks is both a benefit and frustration for the BBICs. A benefit because the BBICs provide the banks with a direct link to the community. Small business lending units of banks' are often bypassed by black entrepreneurs who do not feel comfortable approaching banks because they are not familiar with credit policies. Nor do businesses feel that banks are entirely comfortable dealing with black businesspersons.

The linkage between the local businesses and participating banks' also enhances the banks' reputation with OCC and FRB regulators as well as the banks' CRA records. However, lender

perception of the BBICs is an inhibitive factor for many lenders. Tony Hansberry, the Director of Finance, remarked that bankers still perceive the BBIC network as a social program and an economic development program. He feels that bankers should look at the program as unique and innovative but treat it the same as other business and economic development programs. Mr. Hansberry went on to state that there is a need to make the participating bankers realize that their investments are not enough, they must be willing to extend themselves even further. He explained that while bankers invest, for the most part they do not participate in actual lending black businesses. Nor are many of them particularly interested in offering other assistance to borrowers.

An asset which the executive director sees as beneficial in the BBICs ability to achieve their goals is the community advisory board. The Board is comprised of community or lay people who sit on the loan approval committee as well. The community advocates and businesspersons serve as a check system for the committee to ensure that the BBICs are responsive to local businesspersons interests. The advisory committee articulates the businesses immediate needs to the committees and the general Board.

## **FUTURE**

The BBIC executive director realizes that the network has not fully matured. Except for the Business Assistance Consortium CDC, the BBICs have a short track record in lending and a limited portfolio. One way they intend to alter this is to become certified by the Small Business Administration (SBA) to make qualified loans and begin to establish a more extensive portfolio. In addition, the BBIC will be converting two of its BBICs into federally sponsored Minority Enterprise Small Business Investment Corporations. Essentially this will allow them to act as venture capitalists and make investments that stand to yield a substantial financial gain.

It is important for the BBIC to expand their programs into other income generating enterprises if they wish to continue expanding the base level of capital available for loans.

The network of BBICs is an innovative program and continued regulators and economic development agencies continue to express interest in it and want to learn how it can be duplicated. I believe this model can be duplicated if the necessary funding is made available by state and private agencies.

1. Office of Comptroller of the Currency and the Board of Governors of the Federal Reserve System "CDCs in Small Business Development and Special Housing Programs", Financial Institutions Community Development Corporations Forum, 13 August 1987, p. 23.
- 2.T. DeMarco Hanberry, Director of Finance, Black Business Investment Board. Text of letter sent which describes the Black Business Investment Board and its programs, 24 April 1989, p. 1.
- 3.Ibid.
- 4.Ibid.
- 5.Ibid.
- 6.Cleve Warren, Executive Director, Black Business Investment Board, telephone interview, April 1989.
7. Office of Comptroller of Currency and Board of Governors of the Federal Reserve System, op. cit., p.24.
8. Florida Black Business Investment Board, Annual Fiscal Report, October 1988, p.5.
- 9.Hansberry, p. 4.
- 10.Florida Black Business Investment Board, Annual Fiscal Report, op. cit., p.2.
11. "Minority lending agency picks up speed," Miami Herald, 17 April 1989, Black Business section.
12. Ibid.
13. Ibid.
14. Warren, interview, op. cit.

Chapter 4  
**NORTH CAROLINA NATIONAL BANK CDC (NCNB CDC):  
Economic and Housing Development**

The North Carolina National Bank CDC (NCNB CDC) is a nonprofit subsidiary of NCNB, Charlotte one of the largest commercial banks in deposits in the country. The CDCs mission is to revitalize inner city neighborhoods. Their revitalization projects have produced residential and commercial development in neighborhoods characterized as 'dying, blighted or decayed.'

**TYPE OF BANK CDC**

North Carolina National Bank (NCNB) was the first bank to be granted permission to organize a wholly owned bank CDC. The banks purpose for organizing a CDC was to promote the revitalization of inner-city residential neighborhoods. The OCC authorized the CDC to undertake a variety of activities in order to carry out redevelopment plans. NCNB Community Development Corporation was allowed to "conduct or contract for research and studies related to community development objectives, ..provide technical assistance to non-profit corporations and others with respect to planning, financing and implementing activities to meet community development **objectives of the city**"(emphasis added).<sup>1</sup> The OCC also permitted the CDC to make loans or grants to other nonprofit corporations.

**ORIGIN**

The NCNB CDC was formed as a result of what the CDC's executive director Dennis Rash terms "a bunch of urban pioneers deeply concerned with preserving an a dying neighborhood in uptown Charlotte."<sup>2</sup> The area these urban pioneers (including Dennis Rash, a number of community activists and architects from the University of North Carolina-Charlotte) were concerned with was the Fourth Ward near the central city of Charlotte. In 1975, this neighborhood had essentially been abandoned with only 13 standing houses and a few older

industrial buildings. There were also vacant and undeveloped land parcels in the Ward. Elderly residents comprised the majority of those still living in the Fourth Ward.

Other Charlotte neighborhoods had undergone urban renewal and residents had been displaced. Not only did the urban pioneers want to redevelop the area, but they wanted it preserved for the residents still living there. Mr. Rash and the other urban pioneers began to hold serious discussions with NCNB in an effort to interest them in channeling resources to help revitalize the Fourth Ward community. The group had persuaded the city to designate the area as a historical district. This designation signified that the district was eligible for redevelopment funds.

NCNB agreed to contribute \$100,000 and syndicate a \$700,000 loan pool for residential renovation and mortgage loans. Interest on the mortgages, administered by the city, were tax exempt which permitted the bank to offer below-market rates.

Despite the incentives of having a major bank and city project financing, developers showed little interest in the Fourth Ward. Undaunted by this, NCNB decided that the project was a worthwhile venture and took it upon themselves to develop the area. In 1977, the bank applied to the OCC to organize a CDC. Permission was granted in 1978 and the bank appointed Dennis Rash as its first president and executive director.

## **FUNDING**

As a wholly owned subsidiary of NCNB Corporation, the CDC is capitalized only by the bank. The NCNB Community Development Corporation was capitalized initially at \$250,000 for operation and administration costs. Project profits are reinvested into the CDC and used to subsidize and fund other projects. Injections of additional capital are deployed by the bank at the request of the CDC if it is deemed necessary.

## **PROJECTS**

NCNB Community Development Corporation has participated in many joint ventures with the City and private developers to revitalize other "blighted" neighborhoods. One of their more recent ventures has been the development of 24, 2-3 bedroom homes which were sold to low and moderate income people. The neighborhood surrounded Johnson C. Smith University in Charlotte.

This project provided a unique opportunity to preserve a dying community by granting new homes and homeownership opportunities to public housing tenants. The prices of the homes ranged from \$41,900 to \$62,150. The City provided the land, 4.7 vacant acres, and up to \$400,000 for second mortgages. The CDC provided first mortgage financing at 8.5%. Project guidelines stipulated that residents would not be required to pay more than 30% of their incomes for housing.<sup>3</sup>

At the time of the project, estimates of Charlotte's housing need indicated that 14,000 families lived in substandard housing or paid more than 30% of their income to be housed. The waiting list for public housing totaled between 2000 and 3000 people. Clearly there was a community need for this type of project. This project was cited by the National Association of Housing and Community Development for excellence in providing "affordable, single homeownership in a neighborhood conducive to family living."<sup>4</sup>

NCNB CDC recently has been involved in the downtown revitalization of Raleigh. The CDC worked with the City in completing its comprehensive redevelopment plans for including designs for a new market area of housing and retail development known as Founders Row. NCNB Community Development Corporation was designated as the master developer by the city which meant that they had right of first refusal for any city owned property and review of developer plans.<sup>5</sup>

The housing developed in the Founders Row project, primarily condominiums, was priced from the low \$90's to \$117,000.<sup>6</sup> The CDCs commercial revitalization strategy also included assisting merchants already located in the area to stay in the area. Space in the newly developed retail market area was offered to small businesses. NCNB CDC also financed the creation of a small business incubator and a shared business center to encourage the growth of small and minority businesses in Raleigh.

One of the CDCs more recent undertakings is a housing project in a low-moderate income, predominately black area of southeast Raleigh. The city has assembled the land and will be providing the short term construction financing. This project offers homeownership opportunities to families who may have had to relocate as a result of escalating land and home prices in the area.

#### **PROJECT IMPACT**

The impact of the CDCs development activity in the Fourth Ward generated a renewed interest not only in the area but in the concept of in-town living. Much of the dilapidated housing in the Fourth Ward was restored, other homes were physically moved into the area, and still other were built new. By 1980, the townhouse project had been completed and was occupied. The CDC made plans to build an additional 27 townhouses.

The NCNB CDCs active marketing efforts and commitment to the renovation and redevelopment of the Fourth Ward served as a major stimulus for encouraging the interest of other developers. In 1981, the project was near the end of completion and the City was able to forecast that new residential construction would be over \$20 million for the year. That amount of reinvestment is a distinct contrast to the \$1.5 million that the CDC spent for rehabilitation and renovation in the first three years.<sup>7</sup> Newly developed housing units being developed ranged in price from

\$30,000 to \$100,000 and were marketed for middle income people and first time homebuyers. Since the CDC's modest beginning of constructing 40 units, 520 housing units have been sold in the Fourth Ward area.

#### **STAFF**

The CDC has an executive director and five full time staff persons. The staff includes specialist in marketing, development, and housing. The staff is also involved in outside community boards and volunteer projects.

#### **THE BOARD OF DIRECTORS**

The Board is made of both community and bank officials. There is also a community advisory committee which advises on project impacts. The Board of Directors serves an advisory role and allows the CDC staff to assume responsibility for final project decisions.

## ANALYSIS AND COMMENT

NCNB CDC has been very active and productive in its eleven years of incorporation. From its unique first project to its current housing and economic development efforts, the CDC has been able to compile an impressive and diverse track record of development projects. NCNB CDCs first project generated a certain amount of controversy with the OCC due to the fact that a number of the Fourth Ward's elderly residents were displaced. The CDCs executive director explained that special mortgage loans were offered (5% purchase price downpayment) to the senior citizens wishing to stay in the renovated apartments. The CDC granted relocation assistance to those unable to afford the renovated units or new townhouses. Despite this dubious beginning, NCNB CDC has remained active in a number of community development efforts.

The CDCs ability to influence aspects of community development seems closely linked to the strong support which it has received from top level management. The top level management including the CEO have been able to implement a workable strategy in pursuing community economic development. Their decision to establish a CDC demonstrated their willingness to take risk with a relatively concept.

NCNB CDC was able to get its initial project underway by hiring an aggressive and committed executive director. He, along with the assistance of long time bank staff members, used the CDC as a tool for revitalizing a virtually abandoned area. The NCNB CDC took responsibility for all the development phases even though it had no experience in this area. Since that time, the CDC has put together a professional staff with specialized skills in different aspects of community economic development such as marketing, housing and small business development. The CDC staff is also very involved in other community and civic activities. Staff members sit on various boards, participate in volunteer programs, and provide technical assistance to community service organizations. Community involvement by the staff serves a purpose that

is twofold. First, the staffs visibility promotes the bank and ensures goodwill within the NCNB's community. Second, community involvement gives the staff a chance to identify community credit needs and begin to explore ways in which the CDC can become involved.

One way in which the CDC has found to become more involved in addressing community needs is through participation in joint venture projects with the other CDCs. The traditional CDCs in the area do not always have the capacity to develop projects. So a traditional CDCs ability to tap into the bank's CDCs skill and expertise is often a critical element in capacity building. Also, since NCNB CDC is a nonprofit, the traditional CDCs are able to benefit from any profits generated by the project. The bank CDC can benefit from working with the traditional CDC as well. Traditional CDCs provide banks with a more comprehensive picture of community changes and emerging community development issues.

Not only has NCNB been established good working relations with other community groups but they have gained the trust of the cities where they have completed projects. Their appointment as master developers in the central city revitalization of Raleigh was unprecedented. This clearly demonstrated the extent to which good working relations are necessary for the bank CDC to achieve its goal of revitalizing central cities. NCNB CDC believes that central city revitalization is both a geographic and symbolic necessity if in each project the CDC's goal is striving to help the community to be the best (Interview- Dennis Rash, April 1989). Also, city's have assembled parcels of land for the CDC so that they can initiate development in some areas where no other developers are interested.

Encouraging other developers to take part in projects has been one of the hindrances to projects moving along as quickly as possible. However, as the CDC has completed development projects, encouraging developer interest has become less of a problem and the CDC no longer has to be

the initiator and sole sponsor of projects. One of the most significant problems the CDC has faced in attempting to influence community economic development has been political changes. New city councils institute new agendas, often making affordable housing or community revitalization secondary issues and allocating resources to other areas of concern not necessarily in the purview of the bank CDC.

## **FUTURE**

The NCNB CDC has been interspersing higher return projects with deeply subsidized projects for sometime. They developed the comprehensive revitalization plans for the Founders Row project and then were able to proceed with a low income housing venture. NCNB CDCs strategy of interspersing the two types of projects is done to create an internal subsidy for future housing development.

NCNB CDC is not constrained to one specific type of project because they have been able to gain experience in different aspects of community development including small business assistance, job creation, and housing rehabilitation. The executive director indicated that the CDC would continue expanding its development capabilities these areas.

1. C.F. Muckenfuss, Deputy Comptroller for Policy Planning, Office of Comptroller of Currency, text of opinion letter to NCNB sent 29 March 1978.
2. Interview with Dennis Rash, NCNB CDC, Charlotte, North Carolina, April 1989.
3. "Housing Loans Touted," The Charlotte Observer, 28 July 1986.
4. "An Affordable-Housing Success," The Charlotte Observer, 15 December 1988.
5. "Nonprofit NCNB Development Group Spurs Downtown Raleigh Renovation," North Carolina, September 1986, p.34-35.
6. Ibid.
7. Philip Morris, "When People Live Close," Southern Living November 1980, pp.90-91.

Chapter 5  
**CHEMICAL COMMUNITY DEVELOPMENT, INCORPORATED:**  
**Housing and Real Estate**

Even without the CDC, Chemical Bank, New York, is considered to be pacesetter in the field of community development sponsorship. In 1987, it donated \$10.15 million to philanthropic enterprises.<sup>1</sup> The Bank provided \$600,000 in grants and donations to local service and housing development groups and initiated a loan pool to provide low-interest loans to low-and-moderate income people for housing. The bank's CDC, Chemical Community Development, Inc., serves to enhance Chemical's reputation as an active supporter of community endeavors. The creation of CDC, however, provides several other important benefits for Chemical Bank that other lending vehicles do not.

**TYPE OF BANK CDC**

Chemical Bank Community, Inc., is a for-profit CDC established by Chemical Bank, New York. The CDCs primary focus is providing financial and technical assistance to community based organizations through a variety of loan and grant programs.

**ORIGIN**

Chemical Bank Community Development, Inc. was incorporated at a time when Chemical Bank was considering a merger with Horizon Corporation in New Jersey. Despite being one of the leaders in community development lending and philanthropy, Chemical was challenged by a community group claiming that the bank was not fulfilling its CRA requirements. As one of the leading financial centers in the country, Chemical was a identifiable target for a challenge. A CRA challenge issued against Chemical might other pressure banks, with less than exemplary lending records, into increasing their community development lending.

However, Chemical was able to point to a number of community development projects it had supported. At the time the bank proceeded to establish a CDC which would provide funds for affordable housing and focus internal reporting aspects of the bank's other community lending units.

## PROJECTS

Chemical Community Development, Inc. was initially capitalized with a \$25 million loan pool to provide low-interest mortgage loans to low income persons. Generally, the activities which Chemical Community Development, Inc. undertake include offering a full range of financial assistance programs for real estate financing. The CDC offers permanent construction loans, construction loans and capital improvement loans. These loans are extended to private market and community based organizations developing affordable single and multi-family housing units. The CDC also supports individual families by offering mortgage and home improvement loans to families in city designated community development neighborhoods.

Chemical Community Development, Inc. is supported by four units of the bank: " Urban Development, which provides construction and permanent financing for multi-family housing; Corporate Social Policy, which administers a recoverable grant program for non-profits to pay for soft costs; Shelter Lending, which provides mortgages and rehab loans for 1-4 family units and Community Policy, which provides construction and interim financing to nonprofit's who have service contracts with government agencies."<sup>2</sup> Among their other support programs is a special Certificate of Deposit (CD) that allows socially-interested investors to make deposits at below-market rates or for longer than normal periods of time. The difference between the special CD and the market rate CDs is used to assist in financing affordable housing projects.<sup>3</sup>

Chemical Bank Housing Opportunities Program also supports the activities of the CDC. This

program administers variable grants for administrative costs of nonprofit organizations through the CDC. It also conducts housing seminars on aspects of housing finance, development, and management. <sup>4</sup>

The recoverable grants program, which is funded by the Corporate Social Policy unit, is the first of its kind. It grants developers of affordable housing no interest loans of up to \$500,000, amortized for 3 or 5 years. Borrowers are expected to repay the loan so that it can be lent out again to other nonprofit's.

Chemical Community Development, Inc. coordinates and markets the activities of the four supporting lending units. The lending departments report their community development loans to the CDC which keeps track of the loans for marketing and CRA purposes.

## **PROJECT IMPACTS**

Because Chemical Community Development, Inc. is new, project impacts can not yet be fully assessed. However, the CDC has extended a "\$2 million line of credit to the Community Service Society (CSS), a financing and technical assistance provider to neighborhood based groups involved in affordable housing development for the Ownership Transfer Project (OTP). Under the OTP, CSS provides low-interest financing to low-income tenants who have organized a cooperative to purchase their building from a landlord or the City...".<sup>5</sup>

Additionally, the CDC has made a \$500,000 interest free loan to the Consumer Farmer Foundation. It has also granted monies to community development intermediaries whose goals are to strengthen communities. Specifically, Chemical Community Development, Inc. purchased a \$1 million unit in LISC's Equity Fund and made a \$500,000 interest free loan to the Pratt Institute for Community and Environmental Development.<sup>6</sup>

## **STAFF**

The core CDC staff is augmented by the staff of its supporting lending units. Projects are approved by the particular lending unit responsible for the activity. The CDC staff has been able draw upon the expertise from other lending unit staff. Their knowledge of lending unit procedures and underwriting criteria is critical to the CDC being able to function as a monitoring unit.

## **THE BOARD OF DIRECTORS**

Chemical Development, Inc. has a seventeen member policy making board of directors which includes both the community and senior banking officials. There is also a technical advisory group made up of 15 members from the community, foundations, and government agencies. Quarterly round table discussions to present updates on the activity progress are sponsored by the CDC and Chemical Bank.

## **ANALYSIS AND COMMENT**

Chemical Bank Community Development, Inc. is unusual in that it was not necessarily organized to specifically make direct equity investments in projects. Although, equity investments is included in its range of activities. The state of New York allows banks to make equity investments without a CDC in place. The primary motivation for organizing the CDC is to have it serve as a coordinator of the banks' internal loan reporting activity. More than one lending unit can be involved in a project. For instance, if the real estate and mortgage lending units are involved in projects, the CDC coordinates administrative tasks for these units and disburses the funding.

The establishment of the CDC signaled a shift in the banks community development strategy. Top level management did not feel that the bank's small donations and grants to local groups was having the desired impact in alleviating problems. Management decided to devote more resources to broader projects and innovative programs and utilized the CDC as its administrative mechanism.<sup>7</sup> However, internal consolidation of this type often masks a banks intention to cut back on community development lending and a bank CDC is a convenient way to obscure the effect.

On a much larger scale, Chemical Development is attempting to impact a broader range of community development projects by investing in intermediaries such as the Local Initiatives Support Corporation and Enterprise. These nonprofit intermediary agencies also provide both technical and financial support for the development of low and moderate income housing by other many local development corporations.

## **FUTURE**

Chemical Community Development, Inc. is still relatively new, but the bank is making the

commitment, financially and managerially, to keep it operational. The CDC is able to offer a wide range of service and programs with the support of the banks other lending units. The CDC structure allows these activities be promoted. Its role as community development loan coordinator and monitor is likely to continue. The CDC also keeps track of the banks' progress towards meeting CRA requirements.

1. "A Formula for Success," American Banker, 28 March 1989, p.29.
2. Balonon,op. cit., p. 27.
3. Chemical Bank of New York, Taking the Next Step, (New York: Chemical Bank), p.6.
4. Ibid.
5. Balonon, op. cit., p.28.
6. Ibid.
7. American Banker, op. cit.

## Chapter 6 CONCLUSION

The three community development corporations examined in this study illustrate the wide range and scope of activities of bank CDCs. Each has a special approach to addressing the community economic development issues on which it chooses to focus. The cases reviewed indicate there are many factors which play a role in bank CDC organizational development and goal achievement. The purpose of the case studies was not to judge them against each other or against a model of my own. Rather, identifying internal and external factors critical to a bank CDCs development and ability to achieve its goals, I draw from the cases three factors critical in achieving their goals. A basis for criteria needed to assess the bank CDC model can be established based upon these factors.

### **1) Strong support and sponsorship of a parent bank and staff**

The leadership of the bank's senior management is a primary factor contributing to the CDC's ability to achieve its goals. The senior management clearly articulates the mission and goals of the organization. Often it takes an active role in the direction and development of CDC programs. In fact, Chief Executive Officers and line officers sit on the Boards of their respective CDCs.

The multi-bank consortium BBICs may not have developed as they have without the aggressive organizing and persistence of the Southeast Bank N.A. Their initial sponsorship of the BAC CDC helped build confidence in the organization and the beginning of a track record which is considered vital in helping CDCs to obtain a broader range of community support.

NCNB Community Development Corporation probably would not exist in its present form without high level corporate support. As its executive director states, "the executive staff and

the CEO have to see themselves as risk takers, entrepreneurs, and have an appreciation of what they can accomplish in the community.”<sup>1</sup>

This sense of being able to accomplish tasks must be communicated all the way down the line to the staff working in the CDC. The CDC directors could not emphasize enough the importance of having the staff involved in community projects. The staffs are encouraged to join other community service organizations and participate in as many community activities as possible.

Clearly, this high level of leadership and support is stressed by the executive directors of each of the CDCs as a major contributor to their development.

**2) Establishment of good working relations with communities, and public sector actors operating in the bank CDCs area.**

The cooperation exhibited in the relationships between the bank CDC, the neighborhoods and the public sector greatly influence the ability to achieve organizational goals of the three CDCs. NCNB's Community Development Corporation development experience suggests it is essential to work with all the parties involved in order to complete development projects. Virtually all of NCNB's projects are done as joint ventures. After successfully spurring redevelopment in the Fourth Ward, NCNB became a sought after partner for other inner city revitalization projects. Subsequent joint ventures helped build their organizational and development capacity and skills. NCNB also consults with community groups when they are about to undertake projects. If the groups have the development capability and are able to realize profits from the project, the bank is willing to bring them in as co-venturers. NCNB CDCs capability has now grown to a point where they are extremely trusted developers by both the cities and their development partners, most from the private sector.

The BBICs have also started to develop greater capacity by co-venturing with the Rouse Company in their new mall development. The BBICs are working with Rouse Company in an attempt to locate minority businesses to a new shopping mall. It is hoped the BBICs' new development entity will assist Rouse in bringing new minority businesses to the mall. Besides building relations with Rouse, a major developer, the BBICs will be able to demonstrate that minority businesses can be valuable, money making enterprises able to fit into large scale commercial developments.

Chemical Bank Community Development, Inc., through its technical assistance and programs established vital working relationships with community development corporations. Chemical taps into the established CDCs and service organizations and provides them with needed funding.

**3) Have a thorough understanding of community credit needs and the bank's role in structuring programs to meet those needs.**

All banks are required to ascertain the credit needs of their local communities. Aside from meeting a regulatory requirement, familiarity with needs of their communities enables banks and their CDCs to be responsive to those needs through their activities. The banks highlighted in this study use their CDCs to respond to the needs in their communities.

Obviously, with communities experiencing a multitude of problems, the banks could have chosen any area in which to concentrate their development resources. Chemical Bank Community Development Inc., decided to target its development funds at providing affordable housing.

After NCNB Community Development Corporation completed its first residential housing project, it moved on to other project areas in need of revitalization. Understanding inner city community revitalization needs hinge on more than just housing, the CDC expanded its efforts into restoring older commercial centers despite their lack of experience in this area.

Obviously, the CDC and its parent bank had confidence in the staff's ability to measure community impacts and needs.

## **OBSTACLES TO CDC GOAL ACHIEVEMENT**

The case studies identified three distinct obstacles each has experienced in attempting to achieve their goals. These obstacles can not necessarily be generalized to all bank CDCs, but they give insight to issues which can constrain project and goal achievement.

### **Changes in City Government**

The biggest obstacle NCNB Community Development Corporation experienced was in city council and government. Changes in government often lead to shifts in the focus of the city's community development agenda. New councils and governing bodies do not want to be locked into long term projects agreed to by their predecessors. Funding for redevelopment areas and infrastructure improvements are shifted from projects at times. When public project funds are shifted from a project where the CDC has also invested, NCNB must attempt to replace those funds with alternative investment or delay the project.

### **Perception**

According to the BBIBs director of finance, the biggest drawback to being organized as a minority investment corporation is the investors are not comfortable with a "special" lending program to black entrepreneurs. Their unfamiliarity and discomfort with the BBIC programs inhibits them from participating fully in the loan programs.

Their reluctance in lending to black businesses is coupled with traditional barriers to credit access for small businesses. Banks have long been reluctant to lend to small businesses because of their limited amount of equity, lack of business skill, and poor loan packaging. The executive director related that even with the number of investing banks in the BBICs, bank loan participation rate is only 16%. Part of this low participation rate is attributable to the banks' motivations for participating in the consortium. If banks perceive investment in the consortium as a way of fulfilling CRA requirements or as a social program, then their participation will be minimal.

At this point in their development, a number of the BBICs lack the capacity to provide the necessary technical assistance and generate a greater volume of loans for their portfolio. Consequently, many of the portfolios have very "safe" deals which reflect the risk aversity of the less mature BBICs.

#### **Limiting Environment**

Because they provide loans, grants, and technical assistance to local CDCs which rely upon government programs, Chemical Bank Community Development, Inc. finds that government subsidy reductions hinder their ability to realize some of their goals. Specifically, cutbacks in programs targeted for housing such as Section 8 have limited the CDC's ability to provide affordable housing. Traditional CDCs are reluctant to commit their resources without government subsidies in projects. Also, the government funding programs which they have come to rely upon for administrative funding have been reduced.

Traditional CDCs which Chemical assists are often lacking certain internal capabilities. Specifically, the staffs of other traditional CDCs are not as experienced or skilled in

community development project work. Chemical's staff observed there is a "lack of depth" if the executive director of local CDCs leaves.

Another important factor which the CDC must consider is the lack of buildable lots within the city. This shortage of lots increases land prices. Because the CDC participates in New York's buildable lot program, which supports the construction of affordable housing on vacant lots, a shortage of lots increases the costs of their participation. Consequently, they must provide more equity funding to local CDCs for the acquisition of the higher priced properties. Unfortunately, the number of lots is decreasing as property costs are increasing to a point where it may no longer be feasible to participate in the program.

#### **WHY SOME BANK CDCs FAIL**

There are several reasons why bank CDCs "fail". The failure is reflected in a CDC's inability to accomplish the goal(s) for which it was established. If the parent bank organized the CDC with the expectation it would undertake a variety of community development activities, then the CDC may collapse under the weight of expectations. New bank CDCs should not be expected to assume more tasks, such as housing and jobs creation, than they have the capacity to accomplish. Even traditional CDCs failed as a result of unrealistic expectations of their capabilities.

Bank CDCs also fail if they are not a top priority within the bank. Again, the motivation behind creating of the CDC plays an important role in determining whether the CDC is going to be operationally successful. If top level bank management does not understand the significance and purpose of a bank CDC, then it will view the CDC as a social "give away" program which drains bank resources and returns very little. Similarly, if the CDC or the

bank changes executive directors or managing staff, they may not understand the goals the CDC is set up to achieve.

Bank CDCs can also fail because of external relations with the local government or traditional CDCs operating in the area. The extent to which local government plays a role in a bank CDCs project makes a major difference in project success. Once bank CDCs begin projects, they rely upon local governments to provide critical project resources such as buildings, land, and additional financial support. If local governments chose to withhold assistance, for example, in loan processing or permit issuance, it results in costly delays for bank CDCs. Local governments can also affect funding from other sources if they are dissatisfied with bank CDC in some way or do not see it as the proper community development vehicle.

Traditional CDCs may not consider bank CDCs as the proper vehicle to achieve greater community economic development. Bank CDCs are not established as competition for existing CDCs even though they are often perceived as such. Traditional CDCs may consider bank CDCs as competition for their development "turf", including project areas and resources. As a result, local CDCs may be unwilling to work with bank CDCs. Clearly, cooperation from both the city and local CDCs is a major factor in whether the bank CDC moves projects forward or fail.

Some bank CDCs do not "fail" but do become inactive. Often bank CDCs are set up to complete one particular project, such as revitalizing one neighborhood, and after that one project activities are suspended. Banks may also feel that the CDC is not necessary to achieve its community development goals which might be achieved through other lending units and programs.

## **PROBLEMATIC ASPECTS**

A critique of the bank CDC model raises several problematic aspects. First, while they are not normally organized at the behest of the community, bank CDCs act on behalf of the community. The amount of actual community control and input is limited to an advisory capacity in most cases. Bank CDCs permit the community to sit on loan review committees, however this usually does not have a tremendous affect on the overall policy goals the bank establishes for the CDC.

Because banks may be selective about their choice of projects, they are not necessarily advocates for the whole community. Bank CDCs do not necessarily promote traditional CDC goals of empowering residents and developing community leaders. In fact, bank CDCs do not necessarily have a built in community constituency. These issues raise a fundamental question about whether bank CDCs can legitimately be called "community" development corporations.

The rules which govern bank CDCs are also somewhat ambiguous in defining criteria for assessing the public purpose of projects. Projects which serve a public purpose are permissible under both the broadly written OCC and FRB regulations. The assumption is that the CDCs activities will primarily benefit the low- and moderate-income members of the community. Banks, in general, are risk averse and cautious about the projects they pursue. Bank CDCs do not necessarily seek out the neighborhoods nor address the issues where there is the greatest need.

Bank CDC regulations are vague regarding the capitalization of CDCs once they are initiated. Bank CDCs are established with varying amounts of capital and lines of bank credit. Their

potential impact and ability to undertake projects can be dependent upon how much financial support banks allocate.

Another problematic aspect of bank CDCs is the lack of formal reporting requirements for separate CDC activities. Bank CDC activities are included in general CRA reporting and are not looked at individually. Consequently there is no way of determining what specific benefits the CDCs have for the community particularly those with to low-and moderate income populations.

### **RECOMMENDED CRITERIA**

Bank CDCs have proven themselves to be useful vehicles for community economic development. With the appropriate structure and implementation, they can provide benefits to both the community and the bank. However, bank CDCs are still relatively unknown tools and some aspects of the model can be strengthened to ensure their continued benefit to community development efforts.

Regulators should establish assessment criteria for bank CDCs which is separate from the parent bank's measurement standards. This type of criteria will help regulators measure the CDC's potential impact and influence on community economic development. A performance checklist of criteria similar to the following, provides a basis for this type of evaluation:

- o The CDC must primarily work with non-profit or other community based development organizations;
- o The CDC must utilizes local, state, and federal government program funding to enhance loans and community development efforts;
- o The CDC must solicit community input provided by an advisory council and/or Board participation;
- o The CDC, in conjunction with other bank lending units, must design programs to meet community credit needs in the area, especially the low-and moderate-income communities;

- o The CDC must be flexible in terms of lending criteria and technical assistance provided to its clientele.<sup>2</sup>
- o The CDC must have well defined and measureable goals and objectives for projects, including estimated costs and relative benefits to the community;
- o The CDC must actively market and advertise its services to the community.

## CONCLUDING REMARKS

From the beginning, the primary purpose of this thesis has been to answer two questions of program content:

- 1) What factors are critical to a bank CDCs organizational development and ability to achieve its goals? and,
- 2) Based upon these critical factors, what are criteria for assessing the bank CDC model's influence on community and economic development?

My fundamental assumption is that bank CDCs and related outside actors can pursue courses of action that enhance their ability to achieve their organizational goals and influence community economic development. Additionally, there are particular factors about bank CDCs themselves that increase their effectiveness in particular settings. The findings of my research suggest that this is indeed the case.

Bank CDCs epitomize the public-private initiatives that are so widely praised as valuable to community development efforts. They are also an untapped resource from which more banks and communities could benefit. They have the potential to significantly impact neighborhoods and communities through establishing CDCs. True, banks can organize a community development department, hire community development specialist, or lend to local nonprofit developers without organizing a CDC. However, CDCs are flexible tools that allow banks to undertake a variety of activities usually prohibited to the bank. They are also valuable means to enhance community development efforts. Perhaps a next step in examining bank CDCs would be to identify why their use is limited and suggest ways to promote the use of the bank CDC concept.

The limited scope of this study makes it impossible to consider all the necessary issues in depth. However, one particular implication of the research is significant: for many reasons,

bank CDCs are worthy of continued examination as viable vehicles for community economic development. Bank CDCs compare to Neal Mayer's description of neighborhood development organizations in that they "play unique roles, attack broadly recognized national problems and pursue goals extensively shared by society as a whole, and demonstrate strong .... performance and longer-term promise." <sup>3</sup>

The three case studies examined in this paper demonstrate the bank CDC concept can be used effectively in low- and moderate- income communities. Ultimately, the expansion of private initiatives like bank CDCs is critical to the revitalization and growth of our nation's communities.

1. Interview with Dennis Rash, NCNB CDC, Charlotte, North Carolina, April 1989.
2. Balonon, op. cit., p.16.
3. Neil S. Mayer, Neighborhood Organizations and Community Development: Making Revitalization Work, (Washington: The Urban Institute Press, 1984), p. 183.

### Bibliography:

- "A Formula for Success." American Banker, 28 March, 1989, p.29.
- "An Affordable-Housing Success," The Charlotte Observer,  
15 December 1988.
- Balonon, Alma. "Bank-Sponsored Community Development Corporations."  
Paper prepared for the Ford Foundation. 11 August 1988.
- Berger, Renee A., Moy, Kirsten S., Peirce, Neal R., Steinbach,  
Carol. Investing in America: Initiatives for  
Community and Economic Development. The  
President's Task Force on Private Sector  
Initiatives, 1982.
- Berndt, Harry E. New Rulers in the Ghetto: the Community Development  
Corporation and Urban Poverty. Connecticut: Greenwood,  
1977.
- Clarke, Robert C. "Bank Investments in Affordable Housing:  
Opportunities and Incentives." Paper presented at  
Opportunities and Issues for Banks in Affordable  
Housing Conference. 3 December 1986.
- Daniels, Belden Hull. Development Finance. A Primer for  
Policymakers: A Critique of  
the Administration's Current Development  
Finance Proposals Rural Center, 1979.
- Doney, M. Brett & Nedzi, Bridget K. "Bank-Sponsored Community  
Development Corporations: A Private Sector  
Initiative for Community Development".  
Paper presented at MIT, 11 May 1983.
- Florida Black Business Investment Board. Annual Fiscal Report,  
October 1988.
- "For beleaguered ghettos, another blow: store flight." Boston  
Globe, 4 November 1989.
- Hansberry, T. DeMarco, Director of Finance, Black Business  
Investment Board. Text of letter sent which  
describes the Black Business Investment Board's  
programs. 24 April 1989
- "Housing Experiment Gets First Residents," Mecklenburg Neighbors,  
24 June 1987, p. 4.
- "Housing Loans Touted," The Charlotte Observer, 28 July 1986.

- Mayer, Neil S. Neighborhood Organizations and Community Development: Making Revitalization Work. Washington, DC: The Urban Institute, 1984.
- Metzger, John T. & Weiss, Marc A. The Role of Private Lending in Neighborhood Development: the Chicago Experience. Northwestern University March 1988.
- "Minority lending agency picks up speed," Miami Herald, 17 April 1989.
- Morris, Philip. "When People Live Close," Southern Living (November 1980): 90-91.
- Muckenfuss, C.F., Deputy Comptroller for Policy Planning, Office of Comptroller of Currency. Text of Opinion Letter issued 29 March 1978.
- "New single-family homes project aimed at moderate income buyers," News and Observer, 2 April 1988.
- "Nonprofit NCNB Development Group Spurs Downtown Raleigh Renovation," North Carolina, November 1986.
- Office of Comptroller of the Currency and Board of Governors of the Federal Reserve System. Financial Institutions Community Development Corporations Forum. 13 August 1987.
- Office of Comptroller of the Currency. National Bank Community Development Corporations: Background Information. November 1988.
- Office of Resource Development, Division of Social and Economic Opportunity. Mass. Executive Office of Community and Development. How to Organize a Community Development Corporation: A Manual for Community Organization. March 1980.
- Pierce, Neal R. & Steinbach, Carol F. Corrective Capitalism: the Rise of America's Community Development Corporations. A Report to the Ford Foundation.
- Turabian, Kate L. A Manual for Writers of Term Papers, Theses, and Dissertations, 4th ed. Chicago: University of Chicago, 1973.
- Vandell, Kerry D., Hodas, Barbara S., Rachel Bratt. Financial Institutions and Neighborhood Decline: A Review of the Literature. Prepared for the Federal Home Bank Loan, November, 1974.

Wuest, John J. "One Bank's Stake in its Community: the Mercantile Story." Paper presented at opportunities and Issues for Banks in Affordable Housing Conference 3 December 1986.

Appendix I:  
OCC Interpretive Ruling Regarding Bank CDCs

Interpretive Ruling 7.7480 Investments in community development projects:

Occasionally banks are asked to contribute to a community development corporation, wherein the bank will receive an equity interest in or evidence of debt which may have value in the future, but which is clearly not a bankable asset by ordinary standards. Such "investment" may be made and charged off as a contribution. If the bank wishes to carry the investment as an asset, the examiners will treat it as permissible under the eighth paragraph of 12 USC 24<sup>1</sup>, provided that the following conditions are met:

- a) The project must be of a predominantly civic, community or public nature and not merely private and entrepreneurial.
- b) The bank's investment in any one project does not exceed 2% of its capital and surplus and its aggregate investment in all such projects does not exceed 5% of its capital and surplus.
- c) Such investments are accounted for on the bank's books under "other assets."

Appendix II:  
FRB Section 225.25 (b) (6) of Regulation Y  
Summary of Regulations Regarding BHC CDCs

A bank holding company may make:

Equity and debt investments in corporations or projects designed primarily to promote community welfare, such as economic rehabilitation and development of low-income areas by providing housing, services or jobs for residents.

- a) The community must be the primary beneficiary of all proposed activities.
- b) The holding company's investment must be a key element in achieving those benefits.

## INTERVIEWS

- Janet Gordon. Office of Comptroller of Currency. Personal Interview, March, 1989.
- T. DeMarco Hansberry. Black Business Investment Board Telephone Interview, April, 1989.
- Jim Lowell. Federal Reserve Board. Telephone Interview, May, 1989.
- Bridget Nedzi. Executive Office of Communities and Development. Telephone, April, 1989.
- Dennis Rash. North Carolina National Bank CDC. Telephone Interview, April, 1989.
- Bob Rosenbloom. Chemical Community Development, Inc. Telephone Interview April, 1989.
- Cleve Warren. Black Business Investment Board. Telephone Interview, April, 1989.