Community Development Capital Initiative (US GFC)

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Abstract

The United States Department of the Treasury responded to the Global Financial Crisis with an economy-wide stimulus package called the "Troubled Asset Relief Program" (TARP) (About TARP). Within the portion of TARP's budget dedicated to bank investments, about $570.1 million was disbursed to Community Development Financial Institutions (CDFIs) in a program called the Community Development Capital Initiative (CDCI) (Sept. 30, 2010 Press Release; Bank Investments). Through the CDCI, the Treasury provided capital to CDFIs, encouraged them to lend to small businesses, and promoted other community-oriented goals (Sept. 30, 2010 Press Release). The CDFIs issued either preferred shares or unsecured subordinated debentures to Treasury at low (two percent) interest rates for the first eight years, and high (nine percent) rates thereafter (Feb. 3 2010 Press Release). Five of the 84 participating CDFIs remain in the program as of August 2019. Only one recipient failed (TARP Update Aug. 2019, p. 2). The financial health of participating CDFIs is viewed to have generally improved after the investments were conducted (GAO July 2016 Report, p. 11). In late 2016 and early 2017, 26 of the participants were allowed to pay back Treasury capital at a discount usually seven or eight percent beneath notional value (TARP Update August 2019, p. 41-43).

Keywords: Capital Injection, TARP, Community Development Financial Institution, Community Development Capital Initiative, United States, Department of the Treasury, Global Financial Crisis

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At a Glance

After the Global Financial Crisis, the U.S. Treasury created the CDCI to serve low-income and underbanked communities by injecting capital into Community Development Financial Institutions (CDFIs). CDFIs were banks, thrifts, credit unions, and loan funds that the Treasury had certified to be eligible for financial and technical assistance through the CDFI program (Sept. 30, 2010 Press Release). The Treasury collaborated with federal regulators to review applications, identify eligible and viable institutions, fund them, monitor participants, and wind down investments (CDCI Application Guidelines). The CDCI program was introduced more than a year after the Capital Purchase Program (CPP), a larger TARP program that provided capital to commercial banks during the crisis (CDCI Program Purpose and Overview; Bank Investments). Most CDCI funding represented a revision to CPP investments that Treasury had already made in banks and thrifts that were CDFIs—but on better terms. The CDCI was also the first crisis-era program available to credit unions.

Throughout 2010, the Treasury purchased either preferred stock shares or unsecured debentures from CDFIs, depending on the type of institution (CDCI Application Guidelines). All participants followed similar capital restrictions and payment schedules, transitioning themselves back to private stakeholders within an 8- to 30-year timeframe (July 2016 GAO Report, p. 6). Through the CDCI, the Treasury extended low-cost capital while prioritizing taxpayer interests within CDFI payment schedules.

Summary of Key Terms

Purpose: "To provide support to Main Street banks, thrifts, and credit unions that lend to small businesses and families in underserved communities." (Sept. 30, 2010 Press Release)

Announcement Date	February 3, 2010 (Feb. 3, 2010 Press Release)
Application Window	February 3, 2010 - April 30, 2010 (CDCI FAQs)
Funding/Exchanges Window	February 3, 2010 - September 30, 2010 (Feb. 3, 2010 Press Release; Sept. 30, 2010 Press Release)
Legal Authority	Emergency Economic Stabilization Act of 2008; Troubled Asset Relief Program (TARP); Dodd-Frank Reform Wall Street Reform and Consumer Protection Act (Dodd-Frank) (About TARP; TARP Programs)
Peak Utilization	~$570.1 million provision of Tier 1, Tier 2 capital; 84 participants (CDCI Program Status)
Eligible Institutions	Certified Community Development Financial Institutions (CDFIs) approved by Treasury and their primary federal regulator (CDCI Application Guidelines)
Administrators	United States Department of Treasury; various federal banking agencies (CDCI Application Guidelines)

Summary Evaluation

The Treasury announced a maximum investment amount of $780.2 million and ultimately disbursed $570.1 million to 84 institutions: 36 banks and thrifts and 48 credit unions through the CDCI program (SIGTARP October 26, 2010 Report to Congress, p. 114). As of August 2019, 79 of the original 84 institutions exited the CDCI program: 51 fully repaid, 26 repurchased early, one went into bankruptcy, and one exited through a merger (TARP Update August 2019, p. 2). Of the five remaining institutions, one partially repaid, one partially repurchased early, and one bank converted its preferred shares into common stock. The outstanding balance stood at $23 million, or four percent of the original disbursement. Due to write-offs, the CDCI is currently estimated to fall $60 million short of full-redemption value—given Treasury assumptions about market risks (TARP Update August 2019, p. 5; Analytical Perspectives, p. 347, 348). Participants showed generally improved financial health after receiving Treasury investments (GAO July 2016 Report, p. 11). In late 2016 and early 2017, 26 of the participants were allowed to pay back Treasury capital at a discount usually at seven or eight percent below notional value (TARP Update August 2019, p. 41-43). The Treasury was criticized for exhibiting poor communication by equivocating the program's objectives—a general criticism of TARP—and failing to collect regular information from the participants themselves (American Banker; SIGTARP April 30, 2014 Report to Congress, p. 11). Though the program is largely over, there is still a need for more scholarship.

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I. Overview

Background

In 1994, Congress passed the Riegle Community Development and Regulatory Improvement Act, which established the Community Development Financial Institution (CDFI) Fund (CDFI Fund Website). The U.S. Treasury Department uses the CDFI Fund to promote local economic development by providing financial and technical assistance to financial institutions that Treasury has certified as CDFIs (CDFI Learn More). CDFI certification requires institutions to conduct at least 60 percent of lending and other economic development activities in areas underserved by traditional financial institutions (Sept. 30, 2010 Press Release). CDFIs can be regulated banks, credit unions, or non-profit loan funds. Treasury financial assistance can be in the form of loans, grants, equity investments, deposits, and credit union shares, which CDFIs are required to match dollar-for-dollar with non-federal funds (CDFI Fund Website). Currently, there are more than 1,000 CDFIs located throughout the United States (CDFI History Graphic).

By late 2008, the Global Financial Crisis was in full swing in the United States. On October 3, 2008, President George W. Bush signed the Emergency Economic Stabilization Act (EESA), which granted Congress the authority to purchase troubled assets from financial institutions (Public Law 110-343). Within the EESA, the Troubled Asset Relief Program (TARP) initially granted the United States Department of the Treasury $700 billion—an amount that was later reduced to $475 billion after the passing of the Dodd-Frank Wall Street Reform and Consumer Protection Act on July 21, 2010 (Public Law 111-203). The Treasury disbursed public funds into five program areas: credit markets, the automotive industry, struggling homeowners, the insurance corporation American International Group (AIG), and the banking sector (TARP Programs). Of the $250 billion of TARP funds disbursed to the banking sector, $780.2 million was allocated to the Community Development Capital Initiative (CDCI) (TARP Programs; SIGTARP October 26, 2010 Report to Congress, p. 114).

In launching the CDCI, Treasury officials emphasized its focus on local financial institutions and their customers. "It's a common misconception that TARP funds only went to large Wall Street firms, but the CDCI program is yet another example of how TARP is providing critical assistance to Main Street financial institutions," noted Herbert Allison, Treasury Assistant Secretary for Financial Stability (Sept. 30, 2010 Press Release). The CDCI arrived at a time when private capital had receded from community development financial institutions' primary funding sources—banks, foundations, and socially motivated investors (March 9, 2010 Press Release). Donna J. Gambrell, Director of the Treasury's CDFI Fund, remarked, "At a time when many institutions have pulled back, CDFIs have actually increased their lending and investments in underserved communities. These CDCI investments will enable community banks, thrifts, and credit unions to spur economic development in the communities that have been hit hardest by the economic downturn" (Sept. 30, 2010 Press Release). The Treasury capitalized CDFIs in an effort to reach their low-income and underbanked clients (Sept. 30, 2010 Press Release).

Program Description

The Treasury first announced the CDCI on February 3, 2010 (Feb. 3, 2010 Press Release). Since its origination, the CDCI was presented as a complement to the already running Capital Purchase Program (CPP), a TARP program that extended "capital to viable financial institutions of all sizes throughout the nation" (Bank Investments). In the initial press release, the CDCI was referred to as a "TARP enhancement," and its capital terms (dividend/interest rates, step-up clauses, diversity of eligible institutions) were explicitly framed as more favorable than the CPP (Feb. 3, 2010 Press Release). CDCI eligibility extended to CPP participants that were registered CDFIs and sought lower-cost capital. The Treasury and Government Accountability Office (GAO) frequently combined CDCI and CPP data in public documents.

The Treasury announced that it was willing to dedicate up to $780.2 million during the application window between February 3 and April 30, 2010—an end date that was pushed back from April 2 (SIGTARP October 26, 2010 Report to Congress, p. 114; Feb. 3, 2010 Press Release; CDCI FAQs, p. 2). Transactions took place between February 3, 2010 and September 30, 2010 (Sept. 30, 2010 Press Release). These purchases were conducted with Treasury funds, and the CDFI liabilities and equity were kept on the federal government's balance sheet (Brooking Discussion, p. 17).

To review applications and actively monitor its capital injections, the Treasury partnered with one or more federal regulators: the Federal Deposit Insurance Corporation (FDIC), Board of Governors of the Federal Reserve System, Office of the Comptroller of the Currency (OCC), National Credit Union Administration (NCUA), and Office of Thrift Supervision (OTS) (CDCI Application Guidelines, p. 1).[2] These partnerships were necessary because different financial institutions fell under the jurisdiction of different federal regulators (p. 1).

Eligible institutions for the CDCI were U.S. financial institutions certified as CDFIs by the Treasury's CDFI Fund and regulated by a federal banking or credit union agency (CDCI Application Guidelines, p. 1, 2). If an institution was eligible, the relevant federal regulator would make a recommendation to the Treasury about the institution's financial viability prior to the CDCI investment (CDCI FAQs, "CDCI Program"). The regulator would also consider any private capital raised in conjunction with the CDCI capital injection in its viability assessment (CDCI FAQs, "CDCI Program"). Upon receiving applications, the Treasury discussed the CDFI's eligibility and viability with the primary regulator to either deny or accept the application.

Participating CDFIs were subject to extensive terms and conditions set by the Treasury. As long as the Treasury held at least 10% of its initial investment, the CDFI had to allow the

[2] Under §312 of the Dodd-Frank Wall Street Reform and Consumer Protection Act, the Office of Thrift Supervision (OTS) merged with the OCC, the Fed, the FDIC, and the CFPB (Public Law 111-203, §312, p. 147). Though the OTS was listed in the original CDCI documentation, its CDCI responsibilities were spread across the other regulators upon the OTS merger.

Treasury (along with the Treasury's affiliates) to manage, evaluate, or transfer the Treasury's investment (see "Access and Information" from Bank/Thrift Terms, p. 6, 7; Credit Union Terms, p. 4, 5; S corporation Terms, p. 6, 7; Mutual Bank Terms, p. 6). The 10% threshold also entitled the Treasury to examine and make copies of the CDFI's corporate books, and to discuss the affairs, finances, and accounts with the CDFI's principal officers.

In addition to data access, there were several covenants that the participating CDFI had to agree to follow. For example, the CDFI had to retain its status as a certified CDFI and needed to provide the Treasury with the certification and documents to verify this status, consent to any Making Home Affordable (MHA) modification made by any non-affiliated mortgage servicer, and participate in the Treasury's MHA program under certain circumstances (CDCI Memo, p. 2, 3).

Furthermore, the CDFI was not allowed to engage in any mergers or other significant corporate transaction, subject to undefined exceptions (CDCI Memo, p. 3). It also faced restrictions on common stock repurchases and dividends, including an increase of the aggregate per share dividend over the immediately prior fiscal year.

Capital terms were similar across CDFIs, yet tailored according to the type of institution.

CDCI terms did not explicitly demand any changes to the existing board or management. However, there were limits on executive compensation and bonuses. CDCI participants were subject to the same executive compensation bonuses as other TARP participants (CDCI FAQs, "CDCI Program," p. 2).

The Treasury's shares were generally non-voting. However, except for credit unions, Treasury retained the right to vote on any authorization or issuance of capital shares ranking senior to its investment; any amendment to its rights; or any merger, exchange, dissolution or similar transaction which would adversely affect its rights. In the event of excessive non-repayment of CDCI capital dividend/interest, the Treasury gained voting rights and could place individuals on the board of the CDFI banks or thrifts, banks organized as S corporations, and mutual banks—not for credit unions, however (see "Voting Rights" from Bank/Thrift Terms, p. 4, 5; Credit Union Terms, p. 3; S corporation Terms, p. 5 Mutual Bank Terms, p. 4). If a CDFI wholly defaulted on its debt, the principal and accrued interest were made immediately due and payable once the "event of default" transpired.

The Treasury did not initially have an exit strategy for CDCI investments. The scheduled increase in interest rates was intended to encourage participants to pay back their capital by 2018 (GAO July 2016 Report, p. 14-16). However, in August 2016, shortly after the Government Accountability Office noted the Treasury's lack of an exit strategy, the Treasury announced an early repayment program to help it "dispose of its ownership interests as quickly as practicable" (CDCI Early Repurchase). Under the program, the Treasury would allow participants to repay their capital at "fair value," which in practice meant a discount of nearly seven or eight percent (CDCI Early Repurchase).

Outcomes

Though the Treasury announced a maximum investment amount of $780.2 million, the CDCI ultimately disbursed $570.1 million to 84 institutions: 27 banks and thrifts, nine other banks organized as S corporations, and 48 credit unions (SIGTARP October 26, 2010 Report to Congress, p. 114). The initial application window extended from February through April 2010 (SIGTARP April 20, 2010 Report to Congress, p. 36). By the close of the application window, Treasury received applications from 56 credit unions and 37 banks and thrifts. 36 of 37 bank applications came from CPP participants looking to exchange capital (SIGTARP July 21, 2010 Report to Congress, p. 85, 86).The total number of credit unions and other non-CPP participants that applied for CDCI capital has not been made public, as proposals submitted to primary regulators were kept confidential (CDCI FAQs)).

As of August 2019, 79 of the original 84 institutions exited the CDCI program: 51 fully repaid, 26 repurchased early, one went into bankruptcy, and one exited through a merger. Of the five remaining institutions, one partially repaid, one partially repurchased early, and one bank converted its preferred shares into common stock (TARP Update Aug. 2019, p. 2).

Premier Bank failed in early 2013 (TARP Update Aug. 2019, p. 42). SIGTARP arrested the Chairman of the Board, along with two other board members and the bank president on charges of bank fraud (SIGTARP July 27, 2017 Report to Congress, p. 56). The bank obtained Treasury funds by falsifying its financial data and misrepresenting information to regulators. Treasury lost $6.7 million in TARP funds, and the bank's failure cost the FDIC an estimated $64.1 million.

Of the original 84 CDFIs, four credit unions and one bank have CDCI investments outstanding with total obligations nearing $23 million (TARP Update Aug. 2019, p. 4). Total projected losses on the CDCI are about $60 million—versus $290 million in late 2010 (TARP Update December 2010, p. 3; TARP Update Aug. 2019, p. 5). These losses come from the Treasury reselling the securities below their original purchase price, and from writing off the capital of one bankrupt institution (TARP Update Aug. 2019, p. 41-43). All other CDCI capital left the Treasury's balance sheet through full repayment, early repurchase, or a merger.

One of the requirements of CDCI participation was the annual capital survey, which was intended to capture (via self-reporting) how the CDFIs used their capital (see "Access and Information" from Bank/Thrift Terms, p. 6, 7; Credit Union Terms, p. 4, 5; S corporation Terms, p. 6, 7; Mutual Bank Terms, p. 6). These surveys were subjective; CDFI officials, in their own words, qualitatively described their use of capital with information not found in objective financial reports. From the 2017 survey of 19 CDCI and seven CPP respondents, the top cited uses of capital include: increasing lending, or reducing lending less than otherwise would have occurred (reported by 73.1%), increased reserves for non-performing assets (reported by 30.8%), and held as non-leveraged increase to total capital (reported by 11.5%) (CDCI/CPP 2017 Use of Capital Survey). According to the subjective surveys of the participants, the CDCI aided CDFIs in managing liabilities as well as assets.

II. Key Design Decisions

1. CDCI was created in the likeness of CPP to complement the CPP. Independent laws and Treasury initiatives supported small businesses thereafter.

Most of the funds invested through the CDCI program went to former CPP participants that exchanged their CPP capital for more affordable CDCI capital (CDCI Program Purpose and Overview). Furthermore, ten CPP exchanges qualified for an additional round of investment beyond the original CPP investment, totaling $100.7 million (SIGTARP October 26, 2010 Report to Congress, p. 114). The majority of participants in the CDCI program were credit unions that had not been eligible for CPP capital (GAO June 2014 Report, p. 3, 4). CDFIs run less lucrative business models than mainstream financial institutions and encounter difficulties in securing long-term, low-cost capital from private investors in a time of crisis (March 9, 2010 Press Release).

The CDCI copied the CPP's architecture while softening key payment factors: the CDCI decreased initial interest/dividend rates from the CPP's five percent to two percent, delayed the step-up clauses from the CPP's five years (after the original investment) to eight years, omitted the requirement on stock warrants, and increased the maximum issuance of government capital from the CPP's three percent of risk-weighted assets to five percent (GAO June 2014 Report, p. 4, 5).

Outside of TARP programs, the U.S. Treasury also supported small businesses through the Small Business Act of 2010, which permitted the Treasury to "make capital investments in eligible institutions in order to increase the availability of credit for small businesses, to amend the Internal Revenue Code of 1986 to provide tax incentives for small business job creation, and for other purposes" (Public Law 111-240). Through this Act, the Treasury launched the State Small Business Credit Initiative (SSBCI) and provided nearly $1.5 billion to states, territories, and municipalities (SSBCI Evaluation, p. 1). Rather than directly injecting capital into financial institutions, the Treasury supported state programs that fell into one of five categories: capital access programs, loan guarantee programs, collateral support programs, loan participation programs, and venture capital programs (p. 10). The SSBCI funded small state programs, which filled in market gaps left by larger federal programs (p. 2).

A variety of CDFI Fund programs followed the CDCI and varied in their capital mechanisms (CDFI Fund Programs Overview). These include monetary awards, training programs, tax credits, grants, and bond guarantee programs.[3]

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[3] Under §1204 of Dodd-Frank, the Secretary of the Treasury was permitted to "establish a multiyear program of grants, cooperative agreements, financial agency agreements, and similar contracts or undertakings to promote initiatives designed: (1.) to enable low- and moderate-income individuals to establish one or more accounts in a federally insured depository institution that are appropriate to meet the financial needs of such individuals; and (2.) to improve access to the provision of accounts, on reasonable terms, for low- and moderate-income individuals" (Public Law 111-203, p. 2130).

2. **The legal authority of the CDCI was granted under the Emergency Economic Stabilization Act of 2008.**

The CDCI was legally authorized by the Emergency Economic Stabilization Act of 2008—specifically Title I: the Troubled Assets Relief Program (Public Law 110-343). The broad definition of (purchasable) "troubled assets" could extend to unsecured subordinated debentures and preferred equity if the Secretary of the Treasury were to secure the approval of the Chairman of the Federal Reserve Board (§3, p. 3766, 3767).

3. **The Treasury made CDCI information publicly available, and equivocated the goal of the program.**

To communicate the CDCI, the Treasury relied heavily on the Internet. Online documentation was robust, and the Treasury website contained CDCI Program Documents, Program Agreements for all participating institutions, Frequently Asked Questions (FAQs) about how to participate, and other announcements (CDCI Webpage). The application guidelines webpage held hyperlinks to the websites of federal regulators, where the program details and an application portal were ultimately accessible (CDCI Application Guidelines).[4] All of the Treasury files were published in either PDF or Excel files. After the application window closed, the Treasury announced the CDCI once more via press release on September 30, 2010 (Sept. 30, 2010 Press Release).

The initial public response to the announcement was mixed because the stated goals of the CDCI were, at first, unclear. As "early public announcements and congressional testimony about the program emphasized that the goal of the program was to increase small business lending," some prospective applicants expressed concern about the relevance of the CDCI to their operations (GAO Jan. 2011 Report, p. 47). For example, the National Credit Union Administration and officials from a credit union industry group stressed that their institutions *did not make small business loans*.[5] In subsequent discussions with these officials, the Treasury assured applicants that the purpose of the CDCI was "mainly to capitalize CDFIs so they could achieve their economic development goals"—irrespective of the operations of the CDFI (GAO Jan. 2011 Report, p. 47).

4. **The Treasury worked with financial regulators to review applications, to monitor outstanding funds, and to wind down investments.**

[4] Federal regulators, such as the Office of the Comptroller of the Currency (OCC), advertised the CDCI using the main policy details of the Treasury's first press release: CDFI requirements, individual participation limits, low and fixed-rate dividends, conversion from CPP, and the absence of stock warrants (OCC Spring 2010 Newsletter, p. 10). The narratives presented by regulators appeared consistent with one another.

[5] It is not clear whether credit union representatives interpreted the CDCI's initial goal of "small business lending" as a prerequisite to receive CDCI funding, or as a required condition upon receiving CDCI funding (GAO Jan. 2011 Report, p. 47).

The Treasury relied on primary financial regulators for assistance through every step of the CDCI's lifespan. First, the Treasury-regulator relationship was beneficial for the Treasury. During the initial application window, potential CDCI participants were required to apply to their regulators (CDCI Application Guidelines, p. 1). The primary regulators then curated these applicant pools, endorsing the best applicants and forwarding them to the Treasury for review (Brookings Discussion, p. 13). The combined staff of the Treasury and the primary regulators sought to pre-screen institutions for eligibility and viability quickly and fairly (p. 14).

The CDCI program also helped primary regulators by strengthening some of the institutions they regulated. In several instances, the CDCI capital prevented prompt corrective action from the primary regulators (BCFCU 2012 Capital Survey; CCFCU 2010 Capital Survey; CCFCU 2011 Capital Survey; NSFCU 2017 Capital Survey).

The Treasury-regulator relationship made it easier for CDFIs to decide whether or not to apply for funding. The regulators decided whether or not the CDCI was an appropriate program for the CDFI in question, so the CDFIs could not expend resources by assembling an application to the Treasury (CDCI Application Guidelines, p. 1).

5. The application window for the CDCI was three months.

The funding window for the program was about three full months: February 3 through April 30, 2010 (CDCI FAQs, "CDCI Program"). This window was short because the CDCI needed to be fully functional within TARP's disbursement period; the Treasury's funding authority expired on October 3, 2010 (Sept. 30 2010 Press Release). The Treasury established the application window with the knowledge that it had a few months (May through September 2010) for application review, funding, and exchanges (CDCI FAQs, "CDCI Program").

6. Federally regulated U.S. CDFIs were eligible to apply, but the Treasury and the regulators selected which ones could participate in the CDCI.

The CDCI was available to "banks, savings associations, bank holding companies, savings and loan companies (which engage in solely or predominantly in activities that are permitted for financial holding companies over relevant law), and federally insured low-income designated credit unions" (CDCI FAQs, "CDCI Program"). The basic premise of the CDCI was a securities sale from a CDFI to the Treasury, and the primary regulator facilitated the transaction at every step. The CDFI first discussed capital needs and the appropriateness of the CDCI with its primary regulator (CDCI Application Guidelines, p. 2). Then, the CDFI applied to its primary regulator (through the primary regulator's website), which then decided whether or not to pass the CDFI's application on to the Treasury. Upon receiving applications, the Treasury discussed the CDFI's eligibility and viability with the primary regulator to either deny or accept the application. For state-regulated credit unions, eligibility and viability were decided jointly by state and federal regulators (CDCI FAQs, "CDCI Program").

All TARP applicants were evaluated comprehensively, and overall CDFI financial health was assessed by capital, assets, management, earnings, liquidity, and sensitivity to risk (so-called "CAMELS" ratings) (Brookings Discussion, p. 13). Total application numbers for the CDCI are unknown.[6] If the CDFI agreed to the Treasury's terms and conditions (including Treasury authority consistent with other TARP legislation), a contract was drawn and signed to commence the sale. Treasury document language does not indicate that the CDFI applicant had room to negotiate funding after receiving preliminary acceptance (CDCI Application Guidelines; CDCI FAQs, "CDCI Program"). Thereafter, the CDFI had to comply with the Treasury's additional reporting requirements and financial restrictions, in addition to the rules issued by the primary regulator.

It is worth noting that the Treasury never listed pre-conditions that would *prohibit* an institution from participating—other than failing to follow the terms outlined in the CDCI application and documentation. Within the press releases, public FAQ documents, application materials, and the summary of terms documents, the Treasury did not address minimum/maximum size of balance sheets, the requirement of participation (once an application is accepted), questions of systemic importance, or any otherwise *conditions of ineligibility*.

7. If primary regulators required capital from private investors, the Treasury was willing to match private capital up to five percent of risk-weighted assets (3.5% for credit unions).

In some cases, the primary regulator required CDCI recipients to first raise capital from private markets before they would be allowed to secure Treasury funding. As described by the Treasury, the regulator could take into account junior private investor capital raised alongside CDCI capital—so long as the private capital was an amount at least equal to the CDCI funding (CDCI FAQs, "CDCI Program"). If CDCI funding was contingent on a private capital raise, the amount of CDCI funding still could not exceed the CDCI program limits: matching private capital up to five percent of risk-weighted assets (3.5% for credit unions). More CDFIs became eligible for the program because the matching capital provision helped them reach a higher level of viability than what would be possible by private capital or Treasury capital alone (February 3, 2010 Press Release).

8. Individual participation limits were dependent on the type of institution.

For banks or thrifts, the "maximum investment amount" was no more than five percent of risk-weighted assets (Bank/Thrift Terms, "Size," p. 2, 3). If the primary regulator required

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[6] Application numbers were reported by some—but not all—regulators. The FDIC reported that it received 64 TARP CDCI applications, forwarded 12 onto the Treasury, and 10 were ultimately enrolled into the CDCI program (FDIC 2010 Annual Report, p. 4). The Fed reported that 320 institutions applying to the Treasury's Small Business Lending Fund *also* applied to refinance TARP CPP and CDCI investments, yet 137 were ultimately approved for CPP/CDCI (Fed 2011 Annual Report). The NCUA reported that 111 credit unions applied to the NCUA for CDCI funding (NCUA 2010 Annual Report, p. 33). While it is a challenge to measure exact program take-up, the bottom line is that the Treasury and other regulators denied many applications.

the bank or thrift to raise private capital, then the bank or thrift had to comply. However, the CDCI funding could not exceed the private capital, and the private capital had to be subordinated to the CDCI preferred shares (p. 2). If the bank or thrift was a CPP participant and wished to exchange CPP preferred stock for CDCI preferred stock, then the bank or thrift had to first pay off any remaining dividend/interest payments from the prior preferred stock; the guidelines on "maximum investment amount" and private capital still applied (p. 3). Generally, the bank or thrift could not have violated any of the CPP terms and conditions before participating in the CDCI (p. 3).

For credit unions, the "principal amount" of CDCI funds was no more than 3.5% of total assets and no more than fifty percent of the capital and surplus (Credit Union Terms, "Size of Offering," p. 1, 2). If the primary regulator required the credit union to raise private capital before raising government capital, then the credit union had to comply (p. 1, 2). However, the CDCI funding could not exceed the newly raised private capital, and the private capital had to be subordinated to the CDCI securities (see "Ranking" on p. 2).

For S corporations, the "maximum investment amount" was no more than five percent of the risk-weighted assets (minus the aggregate capital or principal amount of any outstanding TARP assistance) (S corporation Terms, "Size of Offering," p. 2, 3). If the primary regulator required the S corporation to raise private capital before raising government capital, then the S corporation had to first acquire the private capital. However, the CDCI funding could not exceed the private capital, and the private capital had to be subordinated to the CDCI unsecured subordinated debentures (p. 2). If the S corporation desired to exchange CPP securities for CDCI securities, then the S corporation had to first pay off any remaining dividends/interest payments from the prior CPP securities (p. 3). The guidelines on the "Maximum Investment Amount" and private capital still applied. Finally, the S corporation must not have violated any of the CPP terms (p. 3).

For mutual banks, the "aggregate principal amount" was no more than five percent of the risk-weighted assets (less the aggregate capital or principal amount of any outstanding TARP assistance) (Mutual Bank Terms, "Size of Offering," p. 1, 2). If the primary regulator required the institution to raise private capital before acquiring CDCI capital, then the mutual bank had to acquire the private capital first (p. 1). However, the CDCI funding could not exceed the private capital, and the private capital had to be subordinated to the CDCI unsecured subordinated debentures (p. 2). If the mutual bank desired to exchange CPP unsecured subordinated debentures for CDCI unsecured subordinated debentures, then the mutual bank had to first pay off any remaining dividends/ interest payments from the prior CPP securities (p. 2). The guidelines on the aggregate principal amount and private capital still applied. Finally, the mutual bank could not have violated any of the CPP terms (p. 2).

9. Securities were in the form of preferred shares or unsecured subordinated debentures, and the specific terms of CDCI securities varied according to the capital needs and tax treatment of each type of CDFI.

Treasury purchased different types of securities from different types of CDFIs—dependent on the capital required by the given regulator. Generally, banks issued equity in the form of preferred shares with perpetual terms, which was treated as "Tier 1" capital by federal banking regulators (GAO June 2014 Report, p. 4). Credit unions issued debt in the form of unsecured subordinated debentures, which qualified as "Tier 2" (or "secondary") capital, to comply with the National Credit Union Administration (NCUA) standards (GAO June 2014 Report, p. 5). The dividend and interest rates were determined by the tax treatment of the given institutions.

Banks or thrifts issued perpetual preferred stock shares (Bank/Thrift Terms, "Size," p. 2, 3). For bank holding companies and savings and loan holding companies, the preferred stock was cumulative—meaning that the participating bank would have to pay Treasury all dividends owed before paying dividends on any other securities. For banks and thrifts, the preferred stock was non-cumulative. Dividends were fixed at a two percent rate until the eighth anniversary of the closing date of the investment, and then stepped up to nine percent thereafter (Bank/Thrift Terms, "Dividend Rate," p. 3). Finally, for banks or thrifts, there were no contractual restrictions on transfers of the securities; the Treasury reserved the right to sell or auction off these securities (Bank/Thrift Terms, "Transferability," p. 5).

Credit unions issued unsecured subordinated debentures (i.e., debt) with a maturity of either eight or 13 years from the date of the investment (Credit Union Terms, "Maturity," p. 2). On the date of maturity, the credit union paid back the principal plus accrued and unpaid interest. This debt paid cumulative interest: two percent annually until the eighth anniversary of the closing date of the investment, and nine percent annually thereafter (including nine percent default rate on missed payments from years prior) (Credit Union Terms, "Interest Rate" on p. 2).

S corporations issued unsecured subordinated debentures with a maturity of either 13 years for a bank/savings association, or 30 years for a bank or savings and loan holding company (S corporation Terms, "Maturity," p. 2). On the date of maturity, the S corporation paid back the principal plus accrued and unpaid interest. The CDCI debt issued by S corporations paid cumulative interest, fixed at a 3.1% interest rate until the eighth anniversary of the closing date of the investment, and then 13.8% annually thereafter (S corporation Terms, "Interest Rate," p. 3). The higher rates made up for the fact that S corporations banks do not pay corporate taxes (GAO June 2014 Report, p. 2). Assuming a 35% tax rate, these interest rates equate to two and nine percent, respectively.

Mutual banks issued unsecured subordinated debentures with a maturity of 13 years from the date of investment (Mutual Bank Terms, "Maturity," p. 2). On the date of maturity, the mutual bank paid back the principal plus accrued and unpaid interest. As mutual banks also do not pay corporate taxes, the rates on their debt mirrored the rates on the S corporation debt—3.1% rising to 13.8% after eight years (Mutual Bank Terms, "Interest Rate," p. 3).

10. Participating CDFIs were subject to various terms, and the CDCI securities held seniority within CDFI payment schedules.

The CDFI was required to "make representations and warranties described in various Treasury agreements" (CDCI Application Guidelines, p. 2). Among the conditions to participation in the CDCI was the requirement that "the applicant (and its covered officers and employees) agree to comply with the rules, regulations, and guidance of the Treasury with respect to executive compensation, transparency, accountability and monitoring, as published and in effect at the time of the investment closing."

In the publicly available "summary of terms" documents, the Treasury let applicants know what data the CDFIs were expected to report after receiving CDCI funds (see "Access and Information" from Bank/Thrift Terms, p. 6, 7; Credit Union Terms, p. 4, 5; S corporation Terms, p. 6, 7; Mutual Bank Terms, p. 6). As long as the Treasury held at least 10% of its initial investment, the CDFI had to allow the Treasury (along with the Treasury's affiliates) to manage, evaluate, or transfer the Treasury's investment. The Treasury also had the right to examine and make copies of the CDFI's corporate books, and to discuss the affairs, finances, and accounts with the CDFI's principal officers (see "Access and Information" from Bank/Thrift Terms, p. 6, 7; Credit Union Terms, p. 4, 5; S corporation Terms, p. 6, 7; Mutual Bank Terms, p. 6).

The Treasury reserved the right to request and access the information through the institution's federal regulator. While Treasury funds were outstanding, the CDFI had to deliver an audited consolidated balance sheet of the fiscal year, and audited consolidated statements of income, retained earnings, and cash flows (prepared with generally accepted accounting principles, or, in comparative form from the previous fiscal year) (see "Access and Information" from Bank/Thrift Terms, p. 6, 7; Credit Union Terms, p. 4, 5; S corporation Terms, p. 6, 7; Mutual Bank Terms, p. 6). The CDFI was also required to deliver copies of any quarterly reports given to equity/debt holders. If the CDFI was ever audited or received an assessment on its internal controls, a copy of the assessment ought to be delivered to the Treasury as well.

Finally, the CDFI had to complete an annual survey that detailed how it utilized the capital as well as the effects of the capital on its operations and status—this was known as a "capital survey" (see "Access and Information" from Bank/Thrift Terms, p. 6, 7; Credit Union Terms, p. 4, 5; S corporation Terms, p. 6, 7; Mutual Bank Terms, p. 6). Though there was no language about stress tests or triage within CDCI documents, all TARP participants were expected to maintain "good standing" as part of Treasury's ongoing evaluation of CDCI participants.[7]

[7] "Good standing" refers to "material compliance with all the terms, conditions, and covenants of any TARP financial instrument, but not limited to, executive compensation requirements, reporting requirements, and payment of dividends or interest" (see "CDCI Program" section of CDCI Application Guidelines).

With the exception of credit union capital, the CDCI capital terms required CDCI capital to maintain seniority over comparable securities issued by the CDFIs. This prioritized the repayment of taxpayer dollars amongst other CDFI stakeholders.

Banks/Thrifts issued preferred shares that were senior to common stock and *pari passu* (the same ranking) with existing or future authorized and issued preferred shares, and senior to preferred shares which (by their terms) rank junior to any existing or future authorized and issued preferred shares (Bank/Thrift Terms, "Ranking," p. 3).

Credit unions issued unsecured subordinated debentures that constituted secondary capital accounts rather than equity ownership (Credit Union Terms, "Security," p. 1). Credit unions are mutual organizations whose members are shareholder-depositors (Banks, Credit Unions & Savings Institutions). As such, they do not have common equity investors comparable to those in commercial banks. For credit unions, secondary capital accounts are analogous to common stock, and subordinated debt is a form of secondary capital (June 2014 GAO Report, p. 5). As secondary capital accounts, the CDCI credit union debt was subordinated to all other claims against the credit union, including those of creditors, shareholders, and the National Credit Union Share Insurance Fund (Credit Union Terms, "Ranking," p. 2). The CDCI credit union debt was not subject to restoration or replenishment under any circumstances, and it was available to cover operating losses (that exceeded net available reserves) realized by the credit union (Credit Union Terms, "Ranking," p. 2).

S corporation debt ranked senior to the S corporation's common stock (and any other class of equity permitted to the institution by law) (S corporation Terms, "Ranking," p. 2). The S corporations subordinated CDCI debt to: (1.) claims of depositors and other debt obligations to general and secured creditors (if the S corporation was a bank or savings association), or (2.) senior debt (if the S corporation was a bank or savings and loan holding company).

Mutual bank debt ranked senior to mutual capital certificates and other capital instruments authorized under state law (Mutual Bank Terms, "Ranking," p. 2). Mutual bank debt could be subordinated to claims of depositors and to the mutual bank's other debt obligations to its general and secured creditors, unless these obligations were made explicitly *pari passu* or subordinate to the CDCI securities.

11. Dividends/Pricing terms were standardized across all participants, and fixed step-up clauses were applied.

All interest payments were on a synchronized schedule (payments are made quarterly on February 15, May 15, August 15, and November 15 of each year—on the first business day on/after these dates) (Bank/Thrift Terms, "Dividend Rate," p. 3; Credit Union Terms, "Interest Rate," p. 2; Mutual Bank Terms, "Interest Rate," p. 3; S corporation Terms, "Interest Rate," p. 3).

Treasury did not mandate any call options on the debt or warrants on the shares due to the EESA's *de minimis* exception, which gave Treasury the right to waive warrant requirements for institutions with Treasury investments of $100 million or less (SIGTARP July 21, 2010 Report to Congress, p. 86).

If the Treasury investment was still standing after eight years, the institution was prohibited from making common stock dividend payments or repurchases.[8] For credit unions, no special dividends could be declared or paid on any share accounts or other capital instruments. Finally, the CDFI could not enter into any transactions with affiliates unless: (1.) the transaction was no less favorable to the institution and its subsidiaries than could be obtained from an unaffiliated third party, or (2.) the transaction was approved by the audit committee or a comparable body of independent directors of the CDFI (see "Affiliate Transactions" from Bank/Thrift Terms, p. 7, 8; Credit Union Terms, p. 5; S corporation Terms, p. 7, 8; "Access and Information" from Mutual Bank Terms, p. 7). In addition to the preliminary agreements, data privileges, and capital caveats, the Treasury relied on independent evaluators to track the CDCI.

The step-up clauses associated with CDCI capital were fixed and transparent from the announcement of the program (July 2016 GAO Report, p. 15). This increase in dividend/interest rates was the Treasury's attempt to transition CDFIs from public to private funding after eight years (p. 15).

12. CDCI executive compensation was congruent with TARP legislation.

CDFIs with company sizes of 1-25 employees could not receive bonuses, depending on the size of the TARP assistance package—with exceptions for grandfathered bonuses. Stock bonuses could only be paid out in 25% increments alongside the repayment of TARP funds (CDCI Memo, "Executive Compensation and Corporate Governance Requirements," p. 1, 2). There were to be no golden parachutes for the senior executives (or five most highly

[8] When the Treasury purchased preferred shares from banks or thrifts, there arose questions of what to do about stock dilution for other shareholders. CDCI literature indicates that one of the acceptable scenarios in which banks or thrifts can repurchase its own shares is if/when CDCI participation dilutes share prices and inadvertently reduces employee benefits as a result (Cumulative Certificate of Designation, "Section 8," p. A-11; Non-cumulative Certificate of Designation, "Section 8," p. A-12). In this case, the CDFI bank/thrift may repurchase shares to offset (but not exceed) the share dilution amount—"consistent with past practice."

compensated employees after them) if there were still TARP funds outstanding. Senior executive bonuses (and those of the next 20 highest paid employees) could be subject to clawback if it was discovered that these bonuses were based on inaccurate metrics. Tax gross-ups could not be paid to the senior executives (or the next twenty most highly compensated employees). The board had to adopt an excessive or luxury expenditures policy and post the policy on the institution's website. The board also had to create a compensation committee of independent directors who reviewed and evaluated compensation plans twice per year to insulate the institution from unnecessary risks, and this committee had to file annual certifications and disclosures. The chief executive officer and chief financial officer had to file annual certifications covering compliance with the executive compensation and corporate governance requirements. If the institution has securities registered with the SEC, then shareholders had to be provided with an annual advisory vote on executive compensation ("say on pay").

13. CDCI securities were non-voting, but in the event of excessive non-repayment of dividend or interest, the Treasury gained voting rights and could replace board members.

The CDCI securities were all issued with non-voting rights. For banks, thrifts, and mutual banks, the exceptions to the "non-voting rights" are class voting rights on: (1.) any authorization or issuance of capital shares ranking senior to the CDCI preferred stock, (2.) any amendment to the rights of CDCI preferred stock, or (3.) any merger/exchange/dissolution/transaction that would adversely affect the rights of the CDCI preferred stock (see "Voting Rights" from Bank/Thrift Terms, p. 4, 5; Credit Union Terms, p. 3; S corporation Terms, p. 5; Mutual Bank Terms, p. 4).

In the event of "excessive non-repayment" (any dividend/interest not paid in-full for eight periods), the Treasury gained voting rights and could place two individuals on the CDFI's board of directors—as was the case for banks/thrifts, S corporations, and mutual banks (see "Voting Rights" from Bank/Thrift Terms, p. 4, 5; Credit Union Terms, p. 3; S corporation Terms, p. 5). Election rights ended when the dividends were paid in full for four consecutive periods. There were no voting or membership rights whatsoever for CDCI debt from credit unions (Credit Union Terms, "Voting Rights," p. 3). Mutual bank debt was subject to additional "state restrictions" (any state law that restricts the voting rights of CDCI debt that cannot be modified, waived, or otherwise removed by the appropriate state authorities) (Mutual Bank Terms, "Voting Rights," p. 4).

14. Events of default included receivership, conservatorship, or liquidation.

If a CDFI wholly defaulted on its debt, the principal and accrued interest were made immediately due and payable once the event of default transpired. If a credit union defaulted, the National Credit Union Administration could place the credit union into receivership, conservatorship, or liquidation (Credit Union Terms, "Remedies Upon Event of Default," p. 3; "Events of Default," p. 5). For state-chartered credit unions, the appropriate Social Security Administration conducted this event (p. 5). S corporations and mutual banks faced similar consequences by their respective regulators (S corporation Terms, "Remedies Upon Event of Default," p. 5; "Events of Default," p. 7; Mutual Bank Terms, "Remedies Upon Event of

Default," p. 4, "Events of Default," p. 6). Bank (or savings and loan) holding companies could declare bankruptcy and place any major bank subsidiary into receivership (S corporation Terms, "Events of Default," p. 7).

15. The Treasury considered various exit options, but decided in 2016 to enable early repurchases at a discount.

Weighing the CDFI interests while protecting taxpayer investments, the Treasury considered several options for each institution to exit the program. In August 2016, after the GAO noted the Treasury's lack of an exit strategy, the Treasury implemented a program that allowed institutions to buy back their capital at a discount (CDCI Early Repurchase).

While the Treasury preferred that the CDFIs simply paid back the investments in full, partial repayment was possible if the amount was the lesser of five percent of the original injection or $100,000 (Robinson (2017), p. 4). The majority of CDFIs paid back by repurchasing the capital outright.

The Treasury conducted auctions as part of its wind-down strategy for the CPP, and acknowledged that this was also an option for CDCI (July 2016 GAO Report, p. 14). However, the possibility of auctions was contingent on investor demand for the securities, the quality of the underlying financial institutions, and the approval of primary regulators (p. 15, 16).

Debt restructuring was also an option, but not with respect to the interest rates on CDCI securities themselves: "Treasury officials noted that, [as of June 2016], they [had] no plans to alter the terms of the program's rates unless a financial institution was distressed and unable to pay the increased rate. Treasury officials stated that the increases were designed to encourage institutions to replace public capital with private capital within a reasonable amount of time (8 years) and were a cornerstone of the CDCI program" (July 2016 GAO Report, p. 15).

Restructuring was only an option for distressed CDCI institutions that were first willing and able to raise new capital from outside investors (or a merger) (July 2016 GAO Report, p. 15). Through the inclusion of a private investor, the Treasury received cash or other securities that might be sold more easily than preferred stock, but the restructured investments were sometimes sold at a discount to par value. Treasury officials noted that the Treasury would approve restructurings for CDCI only if the terms represented a fair and equitable financial outcome for taxpayers.

For the purposes of "winding down TARP programs in a manner that balances speed of exit with maximizing returns to the taxpayer," the Treasury took proposals from CDCI participants to repurchase their outstanding securities at fair value (CDCI Early Repurchase). Since "fair value" was typically[9] calculated at a discount 7 or 8% under the notional value, this provided CDCI participants with an incentive to pay back early; without the discount, they would have a strong incentive to retain the cheap CDCI capital until the step-up date in 2018, when it would suddenly become very expensive. In November 2016, SIGTARP recommended to Treasury that it not indicate what discount the Treasury would accept; this would help the Treasury ensure the highest possible taxpayer repayment (SIGTARP January 27, 2017 Report to Congress, p. 57). This early repurchase initiative accepted applications between August 1 and December 9, 2016 (Extension). According to the GAO report released during this period, each CDFI must have proposed to repurchase at least 50% of their outstanding CDCI securities for the Treasury to sign on (GAO Nov. 2016 Report, p. 10). 26 of the 57 CDCI participants remaining in 2016 took advantage of this early repurchase period (TARP Update August 2019, p. 2, 41-43).

16. Independent assessments on the CDCI were assigned to the U.S. Government Accountability Office and to the Special Inspector General for the Troubled Asset Relief Program.

The status of the CDCI program as a whole was tracked and reported by both the Treasury and the Government Accountability Office (GAO), an independent, non-partisan agency (About GAO). As part of the Emergency Economic Stability Act (EESA), the GAO had to report to Congress every 60 days on the progress of TARP programs (GAO Jan. 2011 Report, p. 2). Some of these reports described the ongoing status of the CDCI in fine detail (ex: discussing the participants' progress through the entire duration of the program). Other GAO reports were broad and tangentially discussed the CDCI as one of many capital programs. Detailed CDCI statistics (number of institutions repaid vs. remaining, amount of Treasury capital outstanding, estimated lifetime cost to the Treasury, etc.) were included in the Treasury's daily TARP updates in early 2011 and monthly reports to Congress after December 2010 (TARP Update Feb. 9, 2011; TARP Update Dec. 2010, p. 3, 23-24).

The EESA established the Office of Special Inspector General for the Troubled Assets Relief Program (SIGTARP) for the purposes of auditing TARP programs (Public Law 110-343 §121, p. 3788-3790; SIGTARP About Us). SIGTARP is a federal law enforcement agency that strives to "prevent fraud and abuse, identify wasteful spending, and drive improvements." SIGTARP's quarterly reports contain financial data on the current status of Treasury's outstanding investments, TARP-related crime, and SIGTARP's ongoing recommendations for the Treasury's programs (SIGTARP April 30, 2014 Report to Congress). These reports contain CDCI investment summaries, details of missed dividend payments, terms of senior securities and dividends, and a history of the Treasury's CDCI contract enforcement (SIGTARP April 30, 2014 Report to Congress, p. 211-215, 249-262).

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[9] One CDFI received a 20% discount; M&F Bancorp, Inc. repurchased its preferred shares at $800 per share on December 20th, 2016 (TARP Update August 2019, p. 2, 41-43).

III. Evaluation

According to SIGTARP, the Treasury failed to enforce mandatory use of capital reporting, so it is challenge to determine whether CDCI funds were used as intended or not (SIGTARP April 30, 2014 Report to Congress, p. 11; American Banker). Robinson (2017) criticizes the CDCI's weakly positive effects on CDFIs' small business lending, but lending was only one of many measures used to assess CDFI financial health (Brookings Discussion, p. 13). Pana and Wilson (2013) finds that credit unions eligible for TARP funds were more likely to participate in CDCI if they were headquartered in the district of a U.S. House Financial Services Committee member. Treasury officials who oversaw the selection process say they sought to head off any political pressure: "all Congressional calls and input were directed to [political appointees] and kept away from those reviewing applications" (Brookings Discussion, p. 13). These officials suggest that all TARP applicants were evaluated comprehensively, and overall CDFI financial health was assessed by capital, assets, management, earnings, liquidity, and sensitivity to risk (so-called "CAMELS" ratings) (Brookings Discussion, p. 13).

The program's primary objective was changed from fostering small business lending (through CDFIs) to broadly helping CDFIs achieve their independent goals. At the program's announcement in February 2010, it was portrayed as a program to help "Community Development Financial Institutions (CDFIs) that *lend to small businesses*[10] in the country's hardest-hit communities" (Feb. 3, 2010 Press Release). At its onset, the Treasury repeatedly advertised the CDCI as a program for "small business lending"—a phrase that occurs several times throughout the initial press release and public messages. After the Treasury heard the concerns of potential CDCI applicants that did not specialize in small business lending, the Treasury revised its message about the CDCI's objective to something more inclusive: "to capitalize CDFIs to carry out their economic development goals" (GAO Jan. 2011 Report, p. 47). After initially claiming that small business lending was the primary objective of the CDCI (and the primary metric of success), Treasury deferred to CDFIs for a subjective measure of "success" via self-reporting.[11] [12] This shift became an issue when CDFIs failed to report their mandatory use of capital because the Treasury did not know what a large portion (in 2012, the *majority*) of CDCI participants were doing with Treasury funds throughout the lifespan of the program (SIGTARP April 30, 2014 Report to Congress, p. 11). The Treasury relied on

[10] Italics are added here for emphasis and are not present in the press release.

[11] This notion is reinforced by the absence of any question about "small business lending" in the annual use of capital surveys (CDCI/CPP 2017 Use of Capital Survey).

[12] In his exit interview, former SIGTARP Neil Barofsky discusses similar issues with the CPP: "What is Treasury's response [to the lack of lending]? They changed the goal. The [new] goal was to make money. The CPP, according to Treasury officials, by any objective measure was a success. What about the objective measure that you announced, to restore lending? It didn't work. But again, if you change your goals along the way you get to declare everything a success. That doesn't make it a good government program" (American Banker).

the CDFIs to set their own goals, failed to hold CDFIs accountable through reporting standards that were mandated by CDCI contracts, and did not enforce its own voting rights after interest/dividend payments were skipped. With respect to the initial objective, limited research shows that the CDCI did not spur CDFIs to extend more small business loans (Robinson (2017)).

In a 2014 quarterly report to Congress, the Special Inspector General for the Troubled Asset Relief Program (SIGTARP) highlighted oversight issues in the Treasury's handling of CDCI. An increasing number of CDCI participants failed to submit the use of capital survey—a mandatory part of receiving Treasury funding (SIGTARP April 30, 2014 Report to Congress, p. 11). Of the 84 CDCI participants, 14 did not send the annual use of capital survey in 2010, 22 in 2011, and 56 in 2012. "Never once in the history of the CDCI program have all 84 CDCI banks and credit unions complied with the contractual requirement to report annually to Treasury on the use of their funds" (p. 10). If the Treasury does not understand the financial decision making of participating institutions, then the Treasury cannot offer sound advice/guidance to help them achieve their subjective goals, or accurately gauge the overall success of this program (SIGTARP April 30, 2014 Report to Congress, p. 11, 12). Former SIGTARP Neil Barofsky complained about this issue in his 2011 exit interview and suggested that the Treasury "should have required lenders to disclose how TARP funds were used" (American Banker).

The Treasury also failed to act consistently on its own right to attend board meetings and appoint directors in the event of consecutive missed interest/dividend payments (SIGTARP April 30, 2014 Report to Congress, p. 13). In the instance of PGB Holding, Inc., the CDCI participant had missed 12 Treasury dividend payments, yet by April 2014, the Treasury had failed to place any Treasury representatives on the company's board (p. 14). On the other hand, when First American International Corp missed enough payments to warrant a Treasury observer at its board meetings, the Treasury requested an observer in February 2013. "The bank rejected Treasury's request, but subsequently paid the missing dividends"; the Treasury's intent to enforce securities contracts led to better compliance. Treasury also sent observers to Tri-State Bank and Carver Bancorp (SIGTARP January 27, 2017 Report to Congress, p. 57, 58).

Despite the equivocation of program goals, some scholars researched the CDCI under the original premise of small business lending. Robinson (2017) analyzes the financial data of CDCI participants and determines that small business loan growth is positively correlated with high levels of bank capital, liquidity, and high ratios of business loans-to-assets (p. 3). Furthermore, positive growth in business loans is associated with declines in asset quality and increases in profitability. Comparing CDCI participants to minority-owned banks, the paper concludes that "growth in small business lending is strongest among CDCI participants, but participation in the CDCI does not ensure stronger growth in small business lending for any year after participation in the CDCI."

On the basis of small business lending growth, the paper dubs the CDCI a "failure," and attributes failure to the lack of financial incentive to encourage participants to originate more small-business loans (p. 12). However, the study lumps all CDCIs together—rather than focus on those CDFIs whose stated purpose is to provide small-business loans—and includes those that specialize in other financial products like mortgage loans or small personal loans.

The financial health of most CDCI participants improved since they received investments. Between the end of 2011 and March 31, 2016—a time when most participants were still in the program—the median of five of six financial health indicators improved (GAO July 2016 Report, p. 11).[13] However, the median of two financial health indicators weakened.

The average institution took about 2,078 days to exit the CDCI.[14] After interviewing CDCI participants, industry insiders, and federal regulators, the GAO offers a few explanations for the program length: CDFIs waited until cheaper capital was available before returning to the private market, relied on CDCI capital to further expand operations, and some were wary of current and future (ex: Basel III regulatory reforms) capital requirements (GAO June 2014 Report, p. 8-10).

Of the institutions still on the Treasury's balance sheet, each appears to use the Treasury for two broad purposes: to comply with one's primary financial regulation, and to expand financial services and products.

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[13] These indicators include: "(1.) the Texas ratio, which helps determine the likelihood of a bank's failure by comparing its troubled loans to its capital and is calculated by dividing a bank's nonperforming assets plus loans 90 or more days past due by its tangible equity and reserves. Lower Texas ratios indicate stronger financial health. (2.) Noncurrent loan percentage, which is the sum of loans and leases 90 days or more past due and in nonaccrual status. Lower noncurrent loan percentages indicate stronger financial health. (3.) The net charge-offs to average loans ratio is the total dollar amount of loans and leases charged off (removed from balance sheet because of uncollectibility), less amounts recovered on loans and leases previously charged off divided by the average dollar value of loans outstanding for the period. Lower net charge-off to average loans ratios indicate stronger financial health. (4.) The return on average assets measure shows how profitable a bank is relative to its total assets and how efficiently management uses its assets to generate earnings. It is calculated by dividing a bank's net income by the average of its assets over a specific period, such as a quarter or year. Higher returns on average assets indicate stronger financial health. (5.) Common equity tier 1 ratio is a bank's equity capital excluding any preferred shares, retained earnings, and disclosed reserves as a share of risk-weighted assets. Higher common equity tier 1 ratios indicate stronger financial health. (6.) Reserve to nonperforming loans are the funds a bank holds to cover loan losses divided by loans that are 90 days or more past due. Higher reserves to nonperforming loans indicate stronger financial health."

[14] This number does not include the five remaining CDCI participants. This number was calculated from the TARP Update July 2019 (p. 41-43)

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