



NATIONAL FEDERATION OF
COMMUNITY DEVELOPMENT CREDIT UNIONS

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To: Community Banking Advocates
From: Cliff Rosenthal, Executive Director
Re: Creation of a "Neighborhood Banking Corporation" (NBC)
Date: March 8, 1988

As you know, the push by banks to acquire expanded powers has given focus to proposals for expanded CRA and consumer protection measures. In this spirit, NFCDCU would like to present for your consideration and support a proposal to create, with the financial contributions of banks, a new national corporation which will support non-profit, community-based financial institutions serving low-income people.

NFCDCU is a nationwide coalition of 100 credit unions--alternative, community-based, nonprofit financial institutions owned and operated by low-income people in urban and rural areas. Our business is the provision of "basic banking" and lending services to "unbankable" individuals and communities. Our member institutions range in assets from \$100,000 to nearly \$20 million, and have accounted for well over a billion dollars in loans in low-income areas.

In the last five years, community development credit unions (CDCUs) have increasingly been objects, participants, and/or beneficiaries of CRA actions. Under direct or indirect CRA pressure, banks involved in mergers, de-branching, etc. have been persuaded to provide support in a range of forms (investments, grants, technical assistance, etc.) to existing or proposed new credit unions in low-income areas.

NFCDCU believes bank support for CDCUs and other community financial institutions should be greatly and systematically expanded, as a condition for any expansion of bank powers. With minimal outside help, our credit unions have assumed the burden of serving the least profitable sector of the marketplace. While our movement is based on self-help and community financial empowerment, we think banks should share the disproportionate service costs which our credit unions bear--as well as the costs of starting up new institutions to fill the gaps banks are creating as they "upscale."

We have proposed the "Neighborhood Banking Corporation" (NBC) as a new national institution to aggregate and channel bank support for community financial institutions. The NBC would be created by an act of Congress and seeded with a small federal appropriation. Additional permanent capital would be donated by banks. Banks would also be responsible for supplying working capital, in the form of below-market loans and/or investments. The Neighborhood Banking Corporation would function in a manner generally parallel to the Neighborhood Reinvestment Corporation (NRC), which supplies financial and technical support to local Neighborhood Housing Services affiliates.

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While we realize that various pro-consumer banking measures have already been advanced in Congress, we believe that the Neighborhood Banking Corporation is an important companion piece. Without a local financial institution to deliver financial services, a substantial portion of the low-income population will receive little benefit from "lifeline" services. Unfortunately, any consumer measure which increases the cost structure of banks may, in fact, accelerate the trend toward bank branch closings (and may also result in a higher cost of credit). Hence, the need for a strategy which helps develop and maintain financial institutions in low-income neighborhoods.

We would like both your general reaction, as well as specific suggestions, as soon as possible, so that we can formulate an appropriate legislative piece.

Please write or call us (outside New York: 800-437-8711) with your comments and questions at your earliest convenience.

Proposal to Establish the
NEIGHBORHOOD BANKING CORPORATION

Overview.

To meet the banking and credit needs of low-income neighborhoods and consumers, it is proposed that Congress create a national Neighborhood Banking Corporation (NBC). This Corporation will promote the development and expansion of a network of nonprofit community-based financial institutions, specializing in service to low- and moderate-income people.

The Neighborhood Banking Corporation would supplement the protections offered by the Consumer Banking Act of 1988 (sponsored by Rep. Charles Schumer, D--N.Y.) in several important ways.

(1) The Neighborhood Banking Corporation addresses the problem of bank branch closings in low-income areas, by fostering the development of alternative financial institutions. This is important because any mandate for "lifeline" consumer services will still leave large numbers of people unserved, since branch closings have left many neighborhoods without financial institutions to deliver these services.

(2) The Neighborhood Banking Corporation addresses the problem of credit availability in low-income areas. The NBC will provide support to nonprofit financial institutions specifically charged with serving low- and moderate-income people. It will enhance their ability to grant credit to "unbankable" individuals and small businesses. This is not intended to relieve banks of compliance with the Community Reinvestment Act (CRA). Rather, it recognizes that certain loans--by virtue of their small size, inadequate borrower income, etc.--are likely to remain "unbankable" despite any foreseeable strengthening of CRA.

Functions of the Neighborhood Banking Corporation

The Neighborhood Banking Corporation will develop and help capitalize a network of nonprofit financial institutions serving predominantly low-income, "unbankable" or underserved populations.

This network will include community development credit unions (CDCUs), community development loan funds, and other nonprofit financial entities. Approximately 500 of these institutions exist currently, with assets in excess of \$500 million; however, their capabilities and geographic coverage remain very limited, because of financial and technical constraints. The proposed Neighborhood Banking Corporation would broaden the capacity of existing institutions and take an active role in assisting the formation of new

institutions, particularly in areas which have been affected by bank branch closings, the "demarketing" of low-end consumers, and other changes in the banking industry.

The Neighborhood Banking Corporation will generally parallel the Neighborhood Reinvestment Corporation (NRC), the public corporation which has coordinated the development of the extremely successful Neighborhood Housing Services (NHS) network, now numbering hundreds of affiliates across the country.

The NBC will provide supply start-up assistance, management support, and financial support (operating grants, equity contributions, loan or deposit funds, access to secondary markets, etc.) to the local community financial institutions, which--like the affiliates of the NHS network--would be independently incorporated and controlled.

Source of Funds.

The Neighborhood Banking Corporation would be funded primarily by the contributions and loans or investments of the banking industry, particularly: (a) banking companies which utilize new powers granted by Congress (e.g., securities underwriting, real estate, insurance, interstate branching and mergers), and (b) banks which close branches serving predominantly low-income communities. (Preferably, all banks which have closed branches since 1981 would be included.)

Start-up Costs. A small Congressional appropriation (\$2--\$5 million) would be requested for start-up expenses. If adequately capitalized, the NBC would not require annual appropriations.

Permanent Capital. At least \$25 million in permanent capital, or equity, for the NBC should be raised through bank donations. Additional federal capitalization of up to \$6 million could be obtained without any new appropriations, by phasing in, over a five-year period, repayments made to the Community Development Revolving Loan Fund for Credit Unions. [This Fund, established by Congress in 1979, has recently been frozen by an OMB ruling.] The NBC will use the income it earns on its permanent capital to provide operating grants and technical assistance to local community financial institutions (start-ups as well as established entities).

Working Capital. Banks should provide at least \$250 million in working capital through low-cost loans to, or low-yielding investments in, the Neighborhood Banking Corporation. The NBC will channel this working capital into local nonprofit community financial institutions, in the form of loans or deposits. By adding a minimal spread (25--50 basis points) over its cost of funds, the NBC will earn sufficient income to cover its administrative expenses.

Funding Formula

No formula for apportioning contributions and investments among individual banks has as yet been determined. Asset size, revenue generated through use of newly-granted bank powers, number of low-income neighborhood branches closed, and overall CRA rating would appear to be appropriate factors in developing a formula.

Structure

The purposes of the Neighborhood Banking Corporation could likely be accommodated through a variety of structures. The Neighborhood Reinvestment Corporation, a public corporation with a board comprised of representatives of the various financial regulators, is one possible model. A mixed corporation, which includes representatives of the regulators, the banking industry, and low-income consumers, might be appropriate.

The core national operation of the NBC should be kept very modest. Wherever possible, the NBC should carry out its programs and deliver technical assistance through existing nonprofit organizations with the appropriate expertise (e.g., National Federation of Community Development Credit Unions, National Association of Community Development Loan Funds, Woodstock Institute, etc.)

For further information:

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