Spotlight *on* Capital Resources:
Community Development Financial Institutions

Community Development Financial Institutions are a source of debt capital that will play an expanded role in financing community health center capital projects.

Health reform has positioned health centers to play a crucial role in the future health care environment. The Affordable Care Act (ACA) provisions such as Medicaid expansion designed to decrease the number of uninsured populations will put a significant demand on primary care, particularly in low-income communities, where large increases to the number of newly insured are anticipated. These new patients, as well as remaining uninsured populations, will depend on health centers for care, continuing to spur a strong growth phase.

Since 2005, the use of health centers has grown by 50%, requiring an $8.5 billion increase in health center property, plant, and equipment.[1] The ACA's goal is to double the number of health center users from over 21 million currently to 40 million in several years. In order to expand capacity to meet these goals, major investments in facilities is required. In a national capital needs assessment conducted by Capital Link, releasing in the spring of 2014, preliminary results indicate that health centers would need to invest approximately $13.8 billion in capital development to have the capacity to serve 40 million patients, not all of which is planned or funded. Results also suggest that roughly 37% of planned projects have secured funding, leaving a substantial funding gap.[1] Health centers will increasingly need to seek debt financing to meet their capital and operational growth goals in this rapidly changing health care marketplace. Community Development Financial Institutions (CDFIs) are a source of debt capital that will play an expanded role in financing community health center capital projects. While some CDFIs have actively served the health center market for years, many others are emerging sources of capital.

What are Community Development Financial Institutions (CDFIs)?

CDFIs are mission-driven, non-governmental organizations that provide financial products and services to people and communities underserved by traditional financial institutions. Certified by the U.S. Treasury Department's CDFI Fund, CDFIs are financing institutions that have a primary function of promoting economic and community development. They can be banks, credit unions, loan funds, venture capital funds, community development corporations, or microenterprise loan funds, but they have a common goal of bringing capital and credit to low-income communities and are accountable to their communities through board representation. There are more than 900 CDFIs with service areas in all 50 states and in Puerto Rico, serving both urban and rural areas.

What Do CDFIs Do?

CDFIs have an important role in the nation's financial services delivery system because they offer loan products and financial services to communities that are difficult for traditional financial institutions to serve. They provide loans and investments to support the development of quality community facilities, including health centers, housing, and businesses, and provide necessary technical and business assistance to borrowers. Through their lending and investing, CDFIs support businesses that bring essential services such as health care, education, and healthy foods to low-income communities, just to name a few. These businesses are economic catalysts creating jobs and building wealth for low-income communities.

[1] Capital Link, Capital Plans and Needs of Community Health Centers (2014), to be released spring 2014.

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The CDFI Fund

The CDFI Fund is a division within the U.S. Department of Treasury, created in 1994 for the purpose of promoting economic revitalization and community development through investment in and assistance to CDFIs.[2] The CDFI Fund oversees a network of non-traditional lending institutions that share a mission to enhance access to capital in low-income, underserved neighborhoods for the benefit of economically disadvantaged populations. Since its inception, the CDFI Fund has invested more than $1.88 billion to CDFIs, community development organizations, and financial institutions, and allocated almost $36.5 billion under the New Markets Tax Credit program.[3]

The CDFI Fund achieves its purpose by promoting access to capital and local economic growth in the following ways:

1. **The CDFI Program** - Directly investing in, supporting, and training CDFIs that provide loans, investments, financial services, and technical assistance to underserved populations and communities.
2. **The New Markets Tax Credit Program** - Providing an allocation of tax credits to Community Development Entities, which enables them to attract investment from the private-sector and reinvest these amounts in low-income communities.
3. **The Bank Enterprise Award Program** - Providing an incentive to banks to invest in their communities and in other CDFIs.
4. **The Native Initiatives** - Taking action to provide financial assistance, technical assistance, and training to Native CDFIs and other Native entities proposing to become or create Native CDFIs.
5. **The CDFI Bond Guarantee Program** - Issuing bonds to support CDFIs that make investments for eligible community or economic development purposes.

The CDFI Fund also certifies financing entities as "Community Development Entities" (CDEs). Most, but not all CDEs, are also CDFIs. CDEs are eligible to participate in the New Market Tax Credit Program.

How Can CDFIs Support Health Center Growth?

Over the past several years, an increasing number of CDFIs have recognized that health centers have many characteristics that align closely with the CDFI industry's mission and therefore make attractive candidates for investments. The alignment of missions and the prospects for strong health center industry growth resulting from the enactment and implementation of the landmark ACA has raised the profile of health centers in the eyes of CDFIs and the CDFI Fund.

In March 2013, the CDFI Fund announced a new Capacity Building Initiative (www.cdfifund.gov/cbi) focused on training CDFIs on lending to health centers. Beginning in fall 2013 and continuing through February 2015, the program provides basic and advanced training and technical assistance, including 2-day intensive workshops, one-on-one assistance, and an advanced forum for peer learning for CDFIs to establish

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[2] Community Development Financial Institutions Fund

[3] FY14 Program Overview, 10/23/13, www.cdfifund.gov

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and improve lending services that are critical to the needs of health centers. CDFIs will also have access to research and tools that can be used to increase their knowledge of community health centers. The goal of the Capacity Building Initiative is to enhance the capacity of CDFIs to underwrite loans for health centers, providing them with an opportunity to access growth capital to fund the infrastructure required to serve the primary health care needs of up to 40 million low-income residents across the nation.

What Makes CDFIs Different from Conventional Lenders?

CDFIs differ from conventional lending institutions in several important ways:

1. CDFIs have a mission to serve low-income communities. Community and economic development are a priority as opposed to a by-product of lending activities. Many CDFIs started out with a focus on low/moderate income housing development, and now recognize the need for health services for the residents of these developments.
2. CDFIs are not regulated in the same way as commercial banks. CDFIs are often willing to take on a higher level of risk than commercial banks and therefore may be more flexible with underwriting and collateral requirements. CDFIs are often willing to take a subordinated security position to other conventional lenders.
3. CDFIs are able to provide borrowers with high-level technical assistance. Some may have contacts, services, or expertise to help health centers manage a real estate development project.
4. Many CDFIs have access to New Markets Tax Credits, which can provide favorable financing,
5. Some CDFIs may have maximum loan sizes that limit their abilities to provide large loans. However, many have strong working relationships with other CDFIs and will often work together with one, or more, to finance larger projects.
6. Many of the larger banks prefer to work through CDFI intermediaries who bring specialized expertise, rather than act as direct lenders in certain market segments.
7. Some CDFIs have special programs funded by foundations or other investors that provide capital that is specifically structured to meet the needs of health centers, which can make them an attractive source.

A growing number of health centers have taken advantage of CDFI programs over recent years including the New Markets Tax Credit Program, facilities and equipment loan programs, and working capital loans. The financing tools available through CDFIs often provide support for projects that would otherwise be unable to move forward if reliant only on traditional forms of capital. CDFIs are willing to take risks and serve customers with financial products that traditional capital markets are often less likely to provide.

Preparing For Success

The process of applying for financing at a CDFI is similar to that of a traditional lending institution. The first step in the process is to locate one or more CDFIs that have established a service area that applies to your project location. Some CDFIs provide services nationally while others may have service areas that are very

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limited. It's also important to determine whether CDFIs in your area have targeted health centers as a specific focus of their lending. While all CDFIs share certain common characteristics, just like health centers, they have unique areas of expertise and not all will have a focus on health center lending. Ideally, you should target your search on CDFIs that have some experience in health center lending and/or are involved in the CDFI Fund's Capacity Building Initiative. That way you can be assured that they are reasonably knowledgeable about health centers and the challenges you may be facing. CDFIs that promote lending for "community facilities" are the ones that are most likely to work with health centers. To locate CDFIs that are active in your community, visit http://www.cdfifund.gov/awardees/db/index.asp.

Another good source of information about the CDFI industry is the Opportunity Finance Network (www.ofn.org) which is the major trade association for CDFIs. The Opportunity Finance Network has an entire section of its website devoted to financing community health centers: http://ofn.org/financing-community-health-centers.

In general, the health center will need to provide the CDFI with audited financial statements, current year internally prepared financial statements, receivables aging reports, and 12-month forward operating budget. If the health center applicant contemplates a major capital project that will significantly change the health center's operations going forward, then the CDFI lender will typically require a full business plan with pro-forma financial projections for a minimum of five years.

The business plan should address the need for any proposed expansion, and quantify revenue and expense projections. The major elements of a business plan are listed below.

Major Elements of a Business Plan

- History and description of the organization
- Description of model of care and services provided
- Project description/project budget
- Sources and uses (of project funding) statement
- Market description and analysis, including a discussion of market needs, demographics of current and projected patients, and a discussion of competition and trends in the market
- Management and governance of the health center, as well as information on the project team
- Financial/operational assumptions, including:
  - New/expanded services
  - Current and projected staffing (providers and support)
  - Patients and encounters growth projection
  - Payer mix assumptions
  - Projected income statements, balance sheets, and statements of cash flow
  - Key ratio analysis (income statement and balance sheets)

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As mission driven lenders, CDFIs also weigh the community and economic benefits that the project and capital investment is likely to have on low-income neighborhoods and populations. Health centers should be prepared to tell their story describing the positive community impacts that will be realized from the CDFI investment including:

- Creation and retention of permanent jobs
- Creation of construction jobs
- Increase in patients served
- New service offerings
- Addressing health disparities and the social determinants of health that are prevalent in low-income communities

CDFIs, like health centers, are grassroots organizations therefore they like to see community support for the applicant and for the project. Collaborations with state and local government, community groups and foundations are viewed as a plus.

Conclusion

Community health centers are at the forefront of health care reform. Primary health care is viewed as a key component to improving the nation's health and bending the cost curve. Health centers provide high quality, cost effective, culturally competent health care and are therefore positioned for continued strong growth. CDFIs and health centers share many common goals and serve very similar constituents. The opportunity exists for the two industries to grow together and improve the health and well-being of the economically disadvantaged.

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About Capital Link

Capital Link is a non-profit organization that has worked with hundreds of health centers and primary care associations for over 15 years to plan capital projects, finance growth, and identify ways to improve performance. We provide innovative consulting services and extensive technical assistance with the goal of supporting and expanding community-based health care. Additionally, Capital Link works in partnership with primary care associations, the National Association of Community Health Centers, and other entities interested in improving access to capital for health centers. For more information, visit www.caplink.org.

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