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Report to Congressional Committees

July 2016

TROUBLED ASSET RELIEF PROGRAM

Most Community Development Capital Initiative Investments Remain Outstanding

Accessible Version

GAO-16-626

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GAO Highlights

Highlights of GAO-16-626 a report to congressional committees

Why GAO Did This Study

Treasury established CDCI under the Troubled Asset Relief Program (TARP) in February 2010 to help banks and credit unions certified as Community Development Financial Institutions (CDFI) maintain services to underserved communities after the 2007—2009 financial crisis. Eighty-four institutions originally participated in CDCI. The program offered favorable terms for raising capital, including a low dividend or interest rate, an important benefit for CDFIs, which often did not have the same access to capital markets as larger banks. The program's initial dividend or interest rate of 2 percent on investments increases to 9 percent in 2018. The Emergency Economic Stabilization Act of 2008 includes a provision that GAO report at least every 60 days on TARP activities. This report examines (1) the status of CDCI; (2) the financial condition of institutions remaining in the program; and (3) Treasury's strategy for winding down the program.

To assess the program's status, GAO reviewed Treasury reports on the status of CDCI. GAO also used financial and regulatory data to assess the financial condition of institutions remaining in CDCI. Finally, GAO interviewed Treasury officials to examine the agency's exit strategy for the program and interviewed representatives from five trade associations whose member institutions received CDCI capital.

GAO provided a draft of this report to Treasury for its review and comment. Treasury provided technical comments that GAO incorporated as appropriate

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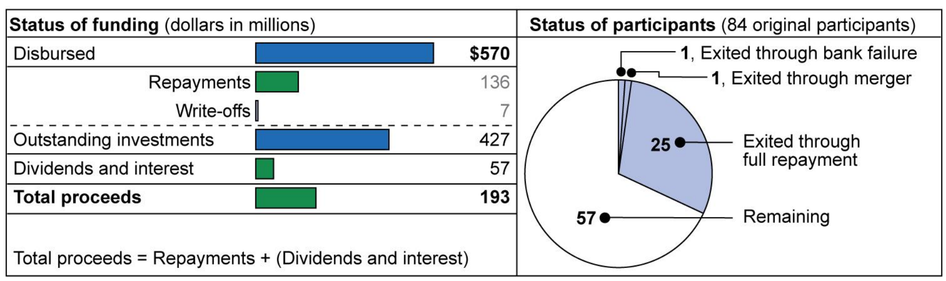
What GAO Found

As of March 31, 2016, the Department of the Treasury (Treasury) had approximately 76 percent of the original Community Development Capital Initiative (CDCI) investment outstanding and 57 institutions remained. Treasury's total investment was about $570 million. Treasury received about $136 million in principal repayments and had written off about $7 million. The program's outstanding investment balance was $427 million. Treasury had received about $57 million in dividend and interest payments from program participants. Treasury's most recent estimate of the program's lifetime cost was about $87 million (as of November 2015). Representatives from trade associations whose member institutions received CDCI capital noted that the program has allowed institutions to maintain and increase lending to their communities.

Status of the Community Development Capital Initiative, as of March 31, 2016



Source: GAO analysis of Treasury data. | GAO-16-626

The financial health of CDCI institutions remaining in the program has improved since receiving Treasury's investments. Overall, the financial condition of banks in CDCI appears to have improved. However, since December 2014, some measures of financial health for these institutions have declined (such as the median for return on average assets). The financial condition of credit unions in CDCI appears to have improved. Finally, nine institutions missed quarterly dividend or interest payments since November 2010 when payments were first due but six of the nine had made up their missed payments as of March 2016.

Although Treasury has not set time frames for exiting all CDCI investments, Treasury officials have studied alternatives to winding down the program, including repayments, auctions, and restructurings. According to Treasury officials and some trade association representatives, many of the remaining institutions are financially healthy and likely will be able to repay the investment before dividend and interest rates increase in 2018. However, some representatives cautioned that some institutions have weaker capital levels and that repaying investments before the rate increases likely would reduce the ability of these institutions to lend in their communities. Some representatives suggested Treasury consider modifying the impending rate increases (for example, by postponing the date). Currently, Treasury officials have no plans to alter the terms of the program unless an institution is distressed and unable to pay the increased rate. Treasury officials plan to continue meeting with CDCI participants and trade associations to further discuss winding down the program.

Contents

Abbreviations

CDCI	Community Development Capital Initiative
CDFI	Community Development Financial Institution
CPP	Capital Purchase Program
Dodd-Frank Act	Dodd-Frank Wall Street Reform and Consumer Protection Act
EESA	Emergency Economic Stabilization Act of 2008
FDIC	Federal Deposit Insurance Corporation
Federal Reserve	Board of Governors of the Federal Reserve System
NCUA	National Credit Union Administration
OCC	Office of the Comptroller of the Currency
TARP	Troubled Asset Relief Program
Treasury	Department of the Treasury

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July 5, 2016

Congressional Committees

The Community Development Capital Initiative (CDCI) was created in February 2010 to help eligible, certified Community Development Financial Institutions (CDFI) and their communities cope with the effects of the 2007—2009 financial crisis.[1] Through the program, the Department of the Treasury (Treasury) provided capital to CDFI banks and credit unions by purchasing preferred equity and subordinated debt from them.[2] Treasury completed funding through CDCI in September 2010 and made approximately $570 million in investments in 84 institutions. CDCI was one of the programs implemented under the Troubled Asset Relief Program (TARP), which gave Treasury the authority to buy or guarantee up to $700 billion, later reduced to $475 billion, of the “troubled assets” believed to be at the heart of the financial crisis. These assets included mortgages, mortgage-backed securities, and certain other financial

[1]CDFIs provide financing and related services to communities and populations that lack access to credit, capital, and financial services. Treasury’s CDFI Fund provides the designation, which allows CDFIs to apply for the CDFI Fund’s financial assistance. Although CDFIs include banks, thrifts, credit unions, loan funds, and venture capital funds, only institutions that have a federal depository institution supervisor (banks, thrifts, and credit unions) could apply for CDCI assistance. The federal supervisors for this program currently are the Federal Deposit Insurance Corporation (FDIC), the Board of Governors of the Federal Reserve System (Federal Reserve), the Office of the Comptroller of the Currency (OCC), and the National Credit Union Administration (NCUA). During the application period, the Office of Thrift Supervision was also a federal supervisor, but it was abolished by the Dodd-Frank Wall Street Reform and Consumer Protection Act (Dodd-Frank Act). See Pub. L. No. 111-203, § 313, 124 Stat. 1376, 1523 (2010) (codified at 12 U.S.C. § 5413).

[2]In this report, “bank” refers to banks, thrifts, and bank or savings and loan holding companies. Some of the institutions in the CDCI program are S-corporations, and that status affects the form of Treasury’s investment. An S-corporation elects to be taxed under subchapter S of chapter 1 of the Internal Revenue Code and thus does not pay income taxes. Instead, the corporation’s income or losses are divided among and passed through its shareholders.

instruments, such as equity investments.[3] CDCI offered favorable capital terms, including a relatively low dividend or interest rate, an important benefit for CDFIs, which may not have the same access to capital markets as larger financial institutions. For example, approved CDFIs issued preferred equity or subordinated debentures to Treasury with initial dividend or interest rates of 2 percent that would increase to 9 percent after 8 years (2018).[4] Treasury has continued to oversee its CDCI investments and collect dividend and interest payments. Some participants have redeemed their securities and exited the program with the approval of their primary federal regulators.

The Emergency Economic Stabilization Act of 2008 (EESA) includes a provision that we report at least every 60 days on TARP activities and performance.[5] We have been monitoring, analyzing, and providing

[3]TARP was authorized by the Emergency Economic Stabilization Act of 2008 (EESA). Pub. L. No. 110-343, 122 Stat. 3765 (codified at 12 U.S.C. §§ 5201-5261). EESA, which was signed into law on October 3, 2008, established the Office of Financial Stability within Treasury and provided it with broad, flexible authorities to buy or guarantee troubled mortgage-related assets or any other financial instruments necessary to stabilize the financial markets. EESA originally authorized Treasury to purchase or guarantee up to $700 billion in troubled assets. § 115(a), 122 Stat. at 3780 (codified as amended at 12 U.S.C. § 5225(a)). The Dodd-Frank Act reduced Treasury's authority to purchase or insure troubled assets to $475 billion. Pub. L. No. 111-203, § 1302(1)(A), 124 Stat. 1376, 2133.

[4]Preferred equity is shares of stock that give the stockholder priority dividend and liquidation claims over common stockholders. Subordinated debentures are a form of debt security that ranks below other senior claims on assets but has priority over all preferred and common shareholders. The securities that Treasury purchased from S-corporations have a 3.1 percent interest rate until the eighth anniversary of the date on which Treasury made the investment, when the rate will increase to 13.8 percent. However, given the tax treatment of S-corporations, these rates equate to effective after-tax rates of 2 percent and 9 percent, respectively (assuming a 35 percent tax rate)—the same rates applied to securities issued by other classes of institutions participating in CDCI.

[5]Pub. L. No. 110-343, § 116(a)(3), 122 Stat. 3765, 3785 (codified at 12 U.S.C. § 5226(a)(3)).

updates on TARP programs, including CDCI.[6] This report examines (1) the status of CDCI, including repayments and other proceeds, as well as investments outstanding; (2) the financial condition of institutions remaining in CDCI; and (3) Treasury's strategy for winding down the program.

To assess the status of CDCI, we analyzed data from Treasury. In particular, we used Treasury's March 2016 Monthly Report to Congress and Investment Program Transaction Report (both published in April 2016) to determine the dollar amounts of outstanding CDCI investments and the number and geographical distribution of remaining participants as of March 31, 2016. We used Treasury's Monthly Reports to Congress to determine when institutions fully repaid the investments. We used data from Treasury's March 2016 Dividends and Interest Report (published in April 2016) to determine the amount of dividends paid. We determined that the financial information used in these reports is sufficiently reliable to assess the status of CDCI based on the results of our audits of TARP financial statements, for fiscal years 2009–2015. As part of our annual audit of the Office of Financial Stability's financial statement we tested Treasury's internal controls over financial reporting.[7] To assess the financial condition of the 57 institutions that remained in CDCI as of March 31, 2016, we analyzed financial and regulatory data from SNL Financial, which provides comprehensive regulatory financial data on financial institutions. We conducted separate analyses for banks and credit unions because the two types of institutions file different regulatory reports and have different financial indicators. We assessed the reliability of SNL Financial data for previous studies by testing required data

[6]See GAO, *Troubled Asset Relief Program: Status of Remaining Investment Programs,* GAO-16-91R (Washington, D.C.: Nov. 3, 2015); *Community Development Capital Initiative: Status of Program Investments and Participants*, GAO-15-542 (Washington, D.C.: May 5, 2015); *Community Development Capital Initiative: Status of the Program and Financial Health of Remaining Participants*, GAO-14-579 (Washington, D.C.: June 6, 2014); *Troubled Asset Relief Program: Treasury Sees Some Returns as It Exits Programs and Continues to Fund Mortgage Programs*, GAO-13-192 (Washington, D.C.: Jan. 7, 2013); and *Troubled Asset Relief Program: As Treasury Continues to Exit Programs, Opportunities to Enhance Communication on Costs Exist*, GAO-12-229 (Washington, D.C.: Jan. 9, 2012).

[7]See GAO, *Financial Audit: Office of Financial Stability (Troubled Asset Relief Program) Fiscal Years 2015 and 2014 Financial Statements*, GAO-16-147R (Washington, D.C.: Nov. 10, 2015).

elements, reviewing existing information about the data and the system that produced them, and interviewing SNL officials. We determined that the financial information we used remains sufficiently reliable for the purposes of our reporting objectives. We also leveraged our past reporting on TARP to inform our assessments of the financial institutions. To examine Treasury's strategy for winding down and exiting the program, we interviewed officials from Treasury and associations representing banks and credit unions that received CDCI capital.

We conducted this performance audit from January 2016 to July 2016 in accordance with generally accepted government auditing standards. Those standards require that we plan and perform the audit to obtain sufficient, appropriate evidence to provide a reasonable basis for our findings and conclusions based on our audit objectives. We believe that the evidence obtained provides a reasonable basis for our findings and conclusions based on our audit objectives.

Background

Created in 2010, CDCI was one of the later TARP programs and was intended to help mitigate the adverse effect of the financial crisis on communities underserved by traditional banks. CDCI is structured much like the TARP Capital Purchase Program (CPP).[8] For example, both programs provide capital to financial institutions by purchasing preferred equity and subordinated debt from them.[9] Institutions are required to make quarterly dividend or interest payments to Treasury until they leave the program. Institutions are expected to repay the investments with the approval of their primary federal bank regulator. However, CDCI differs from CPP in several ways. First, whereas CPP provided assistance to a range of banks, CDCI provided financial assistance only to CDFIs. Second, CDCI provided more favorable capital terms than CPP. For example, certain CDCI investments had an initial dividend or interest rate of 2 percent, compared with 5 percent under CPP. And, the dividend or interest rate increases to 9 percent after 8 years under CDCI, but after 5 years under CPP. The terms of the rates are specified in the agreements

[8]See GAO, *Troubled Asset Relief Program: Capital Purchase Program Largely Has Wound Down*, GAO-16-524 (Washington, D.C.: May 6, 2016).

[9]Subordinated debt are bonds whose claim on income and assets of the issuer in the event of default or the issuer filing for bankruptcy is ranked below the claims of senior bondholders, but above all classes of equity.

between Treasury and the institutions. Finally, CDCI also provided assistance to credit unions, which were not eligible for CPP.

Treasury finalized the last of its $570 million in CDCI investments in September 2010. The 84 original participating institutions were 36 banks and 48 credit unions. Twenty-eight of the 36 banks were CPP participants in good standing in that program and thus were allowed to refinance their CPP shares for a lower rate in CDCI. Of these 28 banks, 10 received additional disbursements under CDCI.

CDCI terms varied depending on the type of institution receiving the capital (see table 1). In general, banks received capital by issuing to Treasury preferred stock representing not more than 5 percent of their risk-weighted assets. The capital they received in return was generally treated as tier 1 capital for regulatory purposes, with a perpetual term. Federal banking regulators classify capital as tier 1—currently the highest-quality form of capital—or tier 2, which is considered weaker in terms of helping institutions absorb losses.[10] Credit unions issued unsecured subordinated debentures totaling not more than 3.5 percent of their total assets. In exchange, Treasury provided participating credit unions with secondary capital that boosted their net worth until 5 years

[10]Tier 1 capital consists primarily of common equity. Tier 2 includes limited amounts of subordinated debt, limited amounts of loan loss reserves, and certain other instruments. Capital regulations issued by the banking regulators in 2013 revise the bank regulatory capital structure and implement higher minimum risk-based capital ratios and a new common equity tier 1 capital requirement, among other things. The new minimum risk-based capital ratios began to apply for certain smaller banking organizations in January 2015. See Regulatory Capital Rules: Regulatory Capital, Implementation of Basel III, Capital Adequacy, Transition Provisions, Prompt Corrective Action, Standardized Approach for Risk-weighted Assets, Market Discipline and Disclosure Requirements, Advanced Approaches Risk-Based Capital Rule, and Market Risk Capital Rule, 78 Fed. Reg. 55340 (Sept. 10, 2013) (FDIC); 78 Fed. Reg. 62018 (Oct. 11, 2013) (Federal Reserve and OCC).

before the maturity date, at which point the debt eligible to be included as secondary capital would be reduced by 20 percent annually.[11]

Table 1: Community Development Capital Initiative Terms, by Institution Type

Type of institution	Initial number of institutions	Type of security	Size of offering	Regulatory capital status	Term or maturity (length from date of investment)	Dividend or interest rate
Bank or thrift	27	Preferred stock	Not more than 5 percent of risk-weighted assets	Tier 1 capital	Perpetual	2 percent for the first 8 years (until 2018); 9 percent thereafter
S-corporation	9	Unsecured subordinated debentures[a]	Not more than 5 percent of risk-weighted assets	Tier 2 capital for a bank or savings association; tier 1 capital for a bank holding company	13 years for a bank or savings association; 30 years for a bank holding company or savings and loan holding company	3.1 percent for the first 8 years (until 2018); 13.8 percent thereafter
Credit union	48	Unsecured subordinated debentures	Not more than 3.5 percent of total assets and not more than 50 percent of capital and surplus	Secondary capital[b]	8 or 13 years	2 percent for the first 8 years (until 2018); 9 percent thereafter

Source: GAO analysis of terms for Community Development Capital Initiative. | GAO-16-626

[a]In the event of liquidation of a company, unsecured subordinated debentures are generally paid after other bonds and debt obligations.

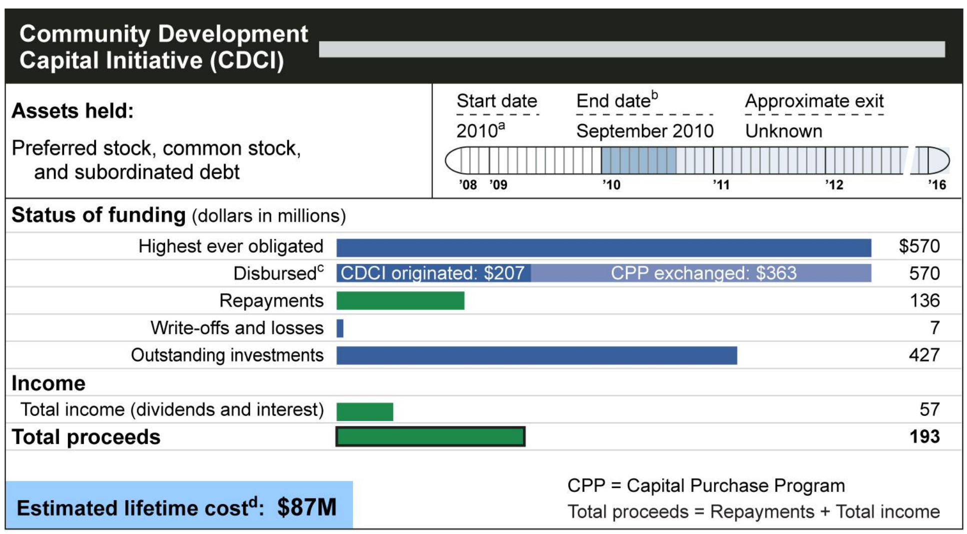
[b]Secondary or supplemental capital is capital beyond that built through retained earnings and provides funding to support lending and other financial services and to absorb losses.

[11]According to NCUA, the purpose of secondary capital (also called supplemental, alternative, or contributed capital) is to provide a further means—beyond setting aside a portion of earnings—for low-income designated credit unions to build capital to support greater lending and financial services in their communities and absorb losses. As a result, the institutions may be less likely to fail. Secondary capital accounts must have a minimum maturity of 5 years, but subject to written approval of NCUA, low-income designated credit unions may request an early redemption exception for all or part of secondary capital accepted from the federal government or any of its subdivisions at any time after it has been on deposit for 2 years. The accounts must be established as uninsured, nonshare instruments. The uninsured secondary capital funds on deposit (including interest paid into the account) must be available to cover operating losses in excess of the low-income designated credit union’s net available reserves and undivided earnings. Funds used to cover such losses may not be replenished or restored to the uninsured secondary capital accounts.

Most of Treasury's CDCI Investments Remain Outstanding

As of March 2016, approximately 76 percent of Treasury's CDCI investment remained outstanding and 57 institutions remained in the program. Treasury's total investment for this program was about $570 million (see fig. 1). Treasury disbursed $207 million through CDCI from July through September 2010 and about $363 million involved exchanges of investments from CPP into CDCI.[12] As of March 31, 2016, Treasury had received approximately $136 million in principal repayments and $57 million in dividend and interest payments from CDCI participants. As of this date, Treasury had written off approximately $7 million, which came from an investment in one institution whose assets were liquidated when its banking subsidiary entered receivership. The program's outstanding investment balance was $427 million.

Figure 1: Status of the Community Development Capital Initiative, as of March 31, 2016



Source: GAO analysis of Treasury data. | GAO-16-626

[a]Treasury announced CDCI in October 2009. The program provided capital to institutions in 2010.
[b]End date is the date on which the program stopped acquiring new assets and no longer received funding.
[c]A total of 28 CPP banks converted from CPP to CDCI. The total amount exchanged into CDCI was about $363 million.
[d]Amount as of November 30, 2015.

[12]Twenty-eight banks were former CPP participants and refinanced their CPP shares for a lower rate in CDCI.

Treasury has lowered its estimates of the program's lifetime cost over the last 4 years as market conditions have improved and institutions have begun to repay their investments. For instance, in November 2010 Treasury estimated the program's lifetime cost at about $287 million, but as of November 30, 2015, estimated lifetime cost was $87 million. Officials of trade associations (that represent community development and minority depository institutions and whose member institutions received CDCI capital) we interviewed noted that CDCI institutions have realized several benefits from the CDCI investments.[13] For example, they stated that CDCI capital allowed many institutions to increase lending, meet customer demand, and provide access to services they otherwise would not have been able to provide.

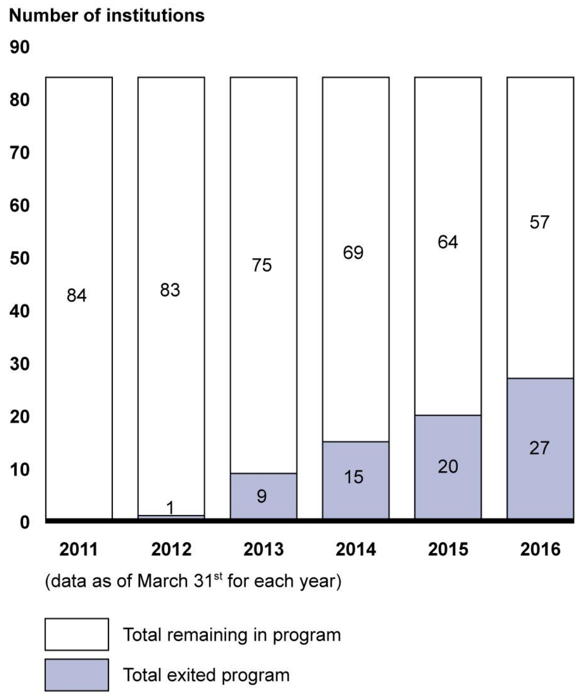
As of March 31, 2016, 57 of the original 84 CDCI participants remained in the program, including 26 banks (5 of which are S-corporations) and 31 credit unions.[14] Among the remaining institutions, 6 had begun to repay the principal on investments they received. The remaining 51 institutions had paid only dividends and interest. The first institution exited the program in March 2012, and since then other institutions gradually have exited the program (see fig. 2). Of the 27 institutions that exited the program, 25 had done so through repayment, 1 merged with another institution, and 1 left the program as a result of its subsidiary bank's failure. Repayments allow financial institutions, with the approval of their regulators, to redeem their preferred shares. Institutions have the contractual right to redeem their shares at any time. However, they must demonstrate that they are financially strong enough to repay the CDCI

[13]Generally, minority depository institutions must have ownership of at least 51 percent by one or more socially and economically disadvantaged individuals. Under section 308 of the Financial Institutions Reform, Recovery, and Enforcement Act of 1989, Congress established certain minority-ownership goals for regulators, including preserving the number of minority depository institutions, preserving their minority character in cases of merger or acquisition, promoting and encouraging creation of new minority depository institutions, and providing for training, educational programs, and technical assistance to prevent insolvency. Pub. L. No. 101-73, § 308, 103 Stat. 183, 353 (codified at 12 U.S.C. § 1463 note). We met with the Community Development Bankers Association, Credit Union National Association, National Association of Federal Credit Unions, National Federation of Community Development Credit Unions, and National Bankers Association.

[14]For one remaining institution, Treasury converted the original investment into shares of common stock. See Department of the Treasury, *Troubled Asset Relief Program, Monthly Report to Congress, March 2016* (Washington, D.C.: Apr. 11, 2016).

investments to receive regulatory approval to proceed with a repayment exit.

Figure 2: Status of Institutions That Received Community Development Capital Initiative Investments, as of March 31, 2016



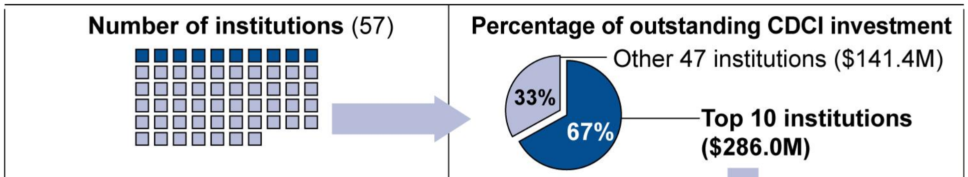
Source: GAO analysis of Treasury data. | GAO-16-626

As of March 31, 2016, the 10 largest remaining institutions were banks and accounted for $286 million (67 percent) of the outstanding investments (see fig. 3).[15] The remaining $141 million (33 percent) was

[15]For nine of the banks, the interest rate is scheduled to increase to 9 percent on the eighth anniversary of the date on which Treasury made the investment. For the remaining bank, the rate is scheduled to increase to 13.8 percent because it is an S-corporation.

spread among the remaining 47 institutions (16 banks and 31 credit unions).[16]

Figure 3: Remaining Community Development Capital Initiative Investments, as of March 31, 2016



Outstanding Community Development Capital Iniative (CDCI) investment by top 10 institutions

	Institution	Location	Investment amount (dollars in millions)	Percentage of total outstanding investment
1	BancPlus Corp.	Ridgeland, MS	$80.91	19%
2	Community Bancshares of Mississippi, Inc.	Brandon, MS	54.60	13
3	Southern Bancorp, Inc.	Arkadelphia, AR	33.80	8
4	Security Federal Corp.	Aiken, SC	22.00	5
5	Carver Bancorp, Inc.	New York, NY	18.98	4
6	The First Bancshares, Inc.	Hattiesburg, MS	17.12	4
7	First American International Corp.	Brooklyn, NY	17.00	4
8	State Capital Corp.	Greenwood, MS	15.75	4
9	Guaranty Capital Corp.[a]	Belzoni, MS	14.00	3
10	Citizens Bancshares Corp.	Atlanta, GA	11.84	3
	Total top 10		**$286.00**	**67%**
	All other CDCI outstanding		$141.44	33%
	All CDCI outstanding		**$427.44**	**100%**

Source: GAO analysis of Treasury data. | GAO-16-626

[a]Institution is an S-corporation.

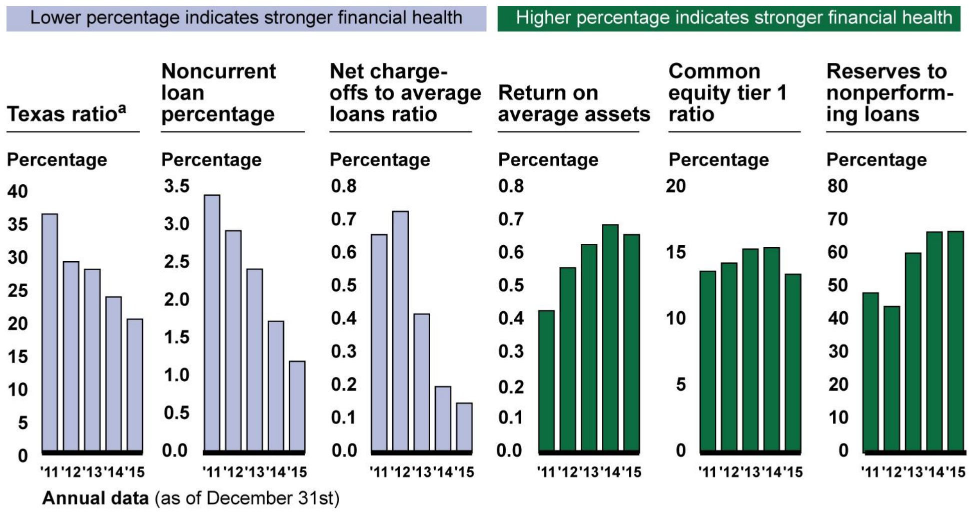
[16]For 12 banks and all 31 credit unions, the interest rate is scheduled to increase to 9 percent on the eighth anniversary of the date on which Treasury made the investment. For the remaining 4 banks, the rate is scheduled to increase to 13.8 percent because they are S-corporations.

Financial Health of Remaining CDCI Institutions Has Improved Since Receiving Investments

Overall, the financial condition of banks and credit unions remaining in the CDCI program as of March 31, 2016, appears to have improved since the end of 2011. As shown in figure 4, the median of five of the six indicators of financial condition that we analyzed for banks generally improved from 2011 to 2015.[17] However, since December 2014 the median of two indicators of financial condition—return on average assets and common equity tier 1 ratio—had weakened.

[17]The six measures are: (1) The Texas ratio 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) Reserves 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.

Figure 4: Median Financial Condition Indicators for Remaining Community Development Capital Initiative Banks, from 2011 through 2015



Source: GAO analysis of SNL Financial data. | GAO-16-626

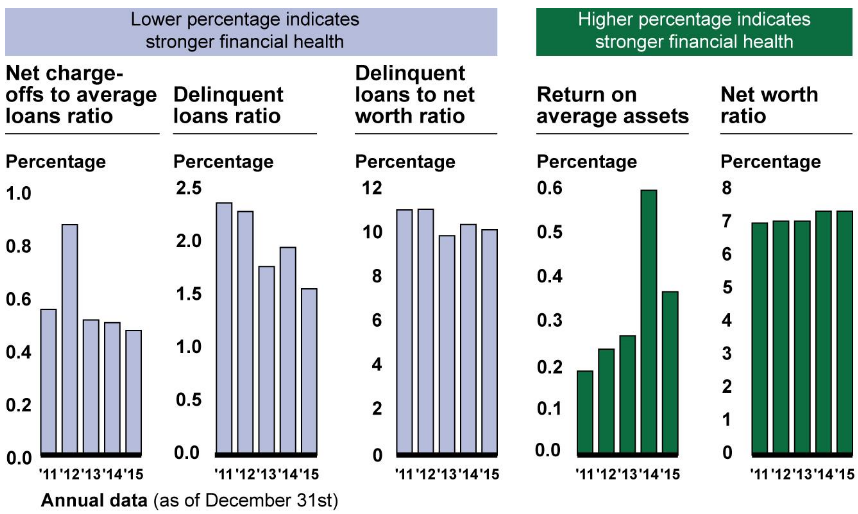
[a]The Texas ratio is defined as nonperforming assets plus loans 90 or more days past due divided by tangible equity and reserves.

Overall, the financial condition of credit unions remaining in the CDCI program as of March 31, 2016, appears to have improved since the end of 2011. As shown in figure 5, the median of all five indicators of financial condition that we analyzed improved from 2011 to 2015.[18] However, since

[18]The five measures are: (1) The net charge-offs to average loans ratio is the total dollar amount of loans charged off (removed from the balance sheet because of uncollectibility), less amounts recovered on loans previously charged off divided by the average dollar value of loans outstanding for the period. Lower net charge-offs to average loans ratios indicate stronger financial health. (2) The delinquent loans ratio is the sum of loans 60 days or more past due divided by total loans. Lower delinquent loans ratios indicate stronger financial health. (3) The delinquent loans to net worth ratio is a credit union's total value of its delinquent loans to net worth. Lower delinquent loans to net worth ratios indicate stronger financial health. (4) The return on average assets measure shows how profitable a company is relative to its total assets and how efficiently management uses its assets to generate earnings. It is calculated by dividing a credit union's net income by the average of its assets over a specific time period, such as a quarter or year. Higher returns on average assets indicate stronger financial health. (5) The net worth ratio is the total of a credit union's regular reserves, any secondary capital, its undivided earnings, and its net income or loss divided by its total assets. Higher net worth ratios indicate stronger financial health.

December 2014 the median of one indicator—the percentage of return on average assets—weakened.

Figure 5: Median Financial Condition Indicators for Remaining Community Development Capital Initiative Credit Unions, from 2011 through 2015



Source: GAO analysis of SNL Financial data. | GAO-16-626

A small number of CDCI institutions have missed quarterly dividend or interest payments and many of these have made up their missed payments. Since November 2010 when dividend and interest payments were first due, nine institutions (seven banks and two credit unions) missed at least one quarterly payment.[19] As of March 31, 2016, six had paid their missed payments and three had unpaid dividends outstanding, two of which have missed their most recent payments.[20] Institutions can elect whether to pay dividends and interest and may not pay for a variety of reasons, including decisions that they or their federal and state

[19]CDCI dividend and interest payments are due on February 15, May 15, August 15, and November 15 of each year, or the first business day subsequent to those dates. The reporting period ends on the last day of the calendar month in which the dividend or interest payment is due. The Dividend and Interest Report published in April 2016 contains the most recent data available for a month in which dividends are due.

[20]See Department of the Treasury, Office of Financial Stability, *Dividends and Interest Report* (Washington, D.C.: Apr. 11, 2016).

regulators make to conserve cash and capital levels. However, investors may view an institution's ability to pay dividends as an indicator of its financial strength and may see failure to pay full dividends or interest as a sign of financial weakness.

Treasury Continues to Consider Various Approaches to Winding Down CDCI and Expects Most Institutions to Exit by Repayments

Although Treasury does not have a specific end date for when it will exit all CDCI investments, Treasury officials continue to consider the interests of participating institutions, such as their financial condition and their plans to exit the program, and protecting taxpayer investments. Treasury also has studied alternatives for winding down the CDCI program, including repayments, auctions, and restructurings. Treasury officials and others expect many of the remaining institutions to exit by fully repaying their investments before September 2018, the latest date on which the interest and dividend rates are scheduled to increase.[21] According to Treasury officials and some representatives from trade associations whose member institutions received CDCI capital, most of the remaining institutions are financially healthy and they expect them to be able to repay the investment before the rate increase.

But representatives from four trade associations—two banking and two credit union—whom we interviewed cautioned that for some institutions with weaker capital levels, repaying the investment before the rate increases likely would have negative consequences. Specifically, the representatives anticipated that financially weaker institutions would not be able to replace the capital and therefore would need to reduce their lending, which in turn would have a negative effect on the communities they serve. Some representatives suggested that Treasury should consider modifying the impending increase to the interest and dividend rates. For example, they said that Treasury could extend the date beyond 2018, reduce the increase below 9 percent, or both. The representatives noted that extending the date beyond 2018 would provide CDCI

[21]According to the definition of "applicable dividend rate" included in the securities purchase agreements, the increase will occur on the eighth anniversary of the date on which Treasury made the investment. Therefore, dividend rates will increase throughout 2018—and no later than September 2018—as institutions mark the eighth anniversaries of their individual agreements. For most banks and credit unions, the rates will increase from 2 to 9 percent. For S-corporation CDCI participants, the rate is scheduled to increase from 2 to 13.8 percent. As of March 31, 2016, five remaining CDCI participants were S-corporations.

participants additional time to raise needed capital. They also noted several benefits of allowing CDCI institutions to maintain their CDCI capital. For example, they anticipated that CDCI capital would allow the remaining institutions to continue to maintain and increase lending, meet customer demand, and provide access to services they otherwise would not be able to provide.

Treasury officials noted that, currently, they have 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.

Treasury continues to consider various options to wind down the CDCI program. Treasury has conducted auctions as part of its wind-down strategy for CPP. Treasury officials acknowledged that selling Treasury's shares of CDCI institutions to other investors is an option for winding down CDCI. However, the success of securities auctions depends largely on investor demand for these securities and the quality of the underlying financial institutions.

Treasury officials noted that restructurings are an option for distressed CDCI institutions. Restructurings allow distressed and troubled financial institutions to negotiate new terms or discounted redemptions for their investments, or both. Raising new capital from outside investors (or a merger) is a prerequisite for a restructuring. With this option, Treasury receives cash or other securities that might be sold more easily than preferred stock, but the restructured investments are sometimes sold at a discount to par value. Again, Treasury has facilitated restructurings as part of its exit strategy for CPP. Treasury officials noted that Treasury would approve restructurings for CDCI only if the terms represented a fair and equitable financial outcome for taxpayers. According to Treasury officials, as Treasury winds down CDCI, as well as the broader TARP program, Treasury prefers to fully exit its outstanding investments rather than exchange or convert investments to new securities that it would continue to hold.

Treasury officials and representatives from trade associations whose member institutions received CDCI capital have discussed possible plans for winding down CDCI on a conceptual level—including repayments, auctions, and restructurings. In addition, Treasury officials told us that they regularly monitor and have direct and substantive conversations with many of the largest remaining 57 institutions about their financial condition and have sought input from CDCI institutions about winding down the program. Treasury officials also told us they plan to continue meeting with these interested parties to discuss winding down the program.

Agency Comments

We provided Treasury with a draft copy of this report for review and comment. Treasury provided technical comments that we have incorporated as appropriate.

We are sending copies of this report to the appropriate congressional committees, the Secretary of the Treasury, and other interested parties. In addition, this report will be available at no charge on the GAO website at http://www.gao.gov.

If you or your staff have any questions about this report, please contact me at (202) 512-8678 or garciadiazd@gao.gov. Contact points for our Offices of Congressional Relations and Public Affairs may be found on the last page of this report. GAO staff who made major contributions to this report are listed in appendix I.

Daniel Garcia-Diaz
Director, Financial Markets and Community Investment

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Appendix I: GAO Contact and Staff Acknowledgments

GAO Contact

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Staff Acknowledgements

In addition to the contact named above, Karen Tremba (Assistant Director), Anne Akin (Analyst in Charge), Bethany Benitez, William R. Chatlos, Lynda Downing, Risto Laboski, Marc Molino, Barbara Roesmann, and Christopher Ross made significant contributions to the report.

Appendix II: Accessible Data

Data Tables

Data Table for Highlights Figure: Status of the Community Development Capital Initiative, as of March 31, 2016

Status of participants	Participants
Total Remaining in program:	57
Merged Institutions:	1
Bankruptcy/Receivership:	1
Full Repayments:	25

Data Table for Figure 2: Status of Institutions That Received Community Development Capital Initiative Investments, as of March 31, 2016

	3/2011	3/2012	3/2013	3/2014	3/2015	3/2016
Total exited program:	0	1	9	15	20	27
Total remaining in program:	84	83	75	69	64	57

Data Table for Figure 3: Remaining Community Development Capital Initiative Investments, as of March 31, 2016

Number of institutions	57

Institution	Location	Amount	Percentage of total outstanding
BancPlus Corporation	Ridgeland, MS	$80.91	19%
Community Bancshares of Mississippi, Inc.	Brandon, MS	$54.60	13%
Southern Bancorp, Inc.	Arkadelphia, AR	$33.80	8%
Security Federal Corporation	Aiken, SC	$22.00	5%
Carver Bancorp, Inc	New York, NY	$18.98	4%
The First Bancshares, Inc.	Hattiesburg, MS	$17.12	4%
First American International Corp.	Brooklyn, NY	$17.00	4%
State Capital Corporation	Greenwood, MS	$15.75	4%
Guaranty Capital Corporation[a]	Belzoni, MS	$14.00	3%
Citizens Bancshares Corporation	Atlanta, GA	$11.84	3%

Institution	Amount	Percentage of total outstanding

(100588)

Institution	Amount	Percentage of total outstanding
Top ten	$286.00	67%
All other CDCI outstanding (47)	$141.44	33%
All CDCI outstanding	$427.44	100%

Data Table for Figure 4: Median Financial Condition Indicators for Remaining Community Development Capital Initiative Banks, from 2011 through 2015

	2011 Q4	2012 Q4	2013 Q4	2014 Q4	2015 Q4
Texas ratio[a]	36.12%	28.88%	27.76%	23.58%	20.21%
Return on average assets	0.43	0.56	0.63	0.69	0.66
Noncurrent loan percentage	3.41	2.94	2.43	1.74	1.21
Net charge-offs to average loans ratio	0.66	0.73	0.42	0.2	0.15
Common equity Tier 1 ratio	13.73	14.35	15.4	15.51	13.5
Reserves to nonperforming loans	48.37	44.24	60.4	66.79	66.96

Data Table for Figure 5: Median Financial Condition Indicators for Remaining Community Development Capital Initiative Credit Unions, from 2011 through 2015

	2011 Q4	2012 Q4	2013 Q4	2014 Q4	2015 Q4
Return on average assets (percent)	0.19	0.24	0.27	0.6	0.37[a]
Delinquent loans ratio	2.38	2.3	1.78	1.96	1.57
Net charge-offs to average loans ratio	0.55	0.87	0.51	0.5	0.47
Net worth ratio	7.01	7.07	7.07	7.37	7.37
Delinquent loans to net worth ratio	11.11	11.14	9.94	10.45	10.21

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