New American Community Loan Fund

OAS Off-Site Sample Report

Note: This sample report is based on actual OAS reports. All names, locations, and other details have been changed.

CDFI Capacity Assessment Report
Organizational Assessment Services

Prepared by: Consultant TBD
Review Conducted: Date TBD

Table of Contents

Executive Summary

NeighborWorks® America conducted an assessment of New American Community Loan Fund (NACLF) in connection with a Community Development Financial Institution (CDFI) capacity building and sustainability initiative. This assessment report is the result of an off-site review of the NACLF documents and telephone communications with its president. The primary focus of this report is to identify issues and provide recommendations relating to the CDFI's capitalization and liquidity.

New American Community Loan Fund is a eight year-old nonprofit, 501(c)(3) organization and is a certified CDFI. Its mission is "*to conduct activities to support the purposes of the New American CDC*". The organization's purpose is to "engage in community and economic development activities that will build secure and successful neighborhoods in the metro area where low to moderate-income people, especially immigrants and refugees, live and work.

To that end, the NACLF promotes business development, affordable housing and home ownership, savings, job development, immigrant community participation, and similar activities that help to empower its core constituency, primarily recent refugees and immigrants. The NACLF also provides loans to support small and micro businesses and development services that help strengthen financial operations.

The NACLF is a subsidiary of the New American CDC (the CDC). Founded in 1945, the CDC's mission is to help refugees and immigrants become productive US citizens by providing comprehensive adjustment services such as language classes, resettlement and job location services, as well as offering programs that foster and encourage cross-cultural understanding. The CDC's activities are heavily subsidized, principally through a Federal grant from the Office of Refugee Resettlement (the U.S. Department of Health & Human Services), as well as through individual, philanthropic and corporate contributions.

As a relatively young CDFI, the NACLF faces many challenges that affect its long-term sustainability, including inadequate staffing, limited lending and operating capital, and lack of clarity about roles, responsibilities and commitment of its parent, the CDC.

Despite these obstacles, the NACLF has achieved the following:

1. Identified an important market niche, and cultivated a presence in this market;
2. Extended approximately 98 loans (through June 30, 2015) totaling more than $790,000; and,
3. Decreased the percentage of the portfolio at-risk and reduced delinquencies.

PRODUCTION/PROGRAM SERVICES

NACLF provides loans to low income and minority entrepreneurs that assist in starting, strengthening and expanding small businesses. The profile of a typical NACLF borrower is a recent immigrant (or refugee) that may (or may not) have prior business experience in their home country and desire to start or expand a business. These clients have been unable to secure traditional bank financing for various reasons, e.g., short, erratic or no operating track record, poor or no business or personal credit history, inadequate or no collateral, small loan size and cultural and language barriers.

NACLF offers flexible underwriting criteria, nontraditional collateral and development assistance to low income entrepreneurs to help start, expand or strengthen a business, including a financial education series, and expert help with recordkeeping, budgeting, accounting, marketing and legal issues. Development services are provided primarily by NACLF's parent, the CDC, and through a network of volunteers. Please see Appendix A for an overview of the NACLF loan products.

LOAN PRODUCTION ACTIVITY

As shown in Figure 1 below, NACLF's loans outstanding nearly doubled in the past three and one-half years, and loan activity (as measured by the number and volume of loans disbursed) has steadily increased. Deployment has improved, from 45 percent (at FYE 2012) to 59 percent at June 30, 2015, but is still relatively low. The major contributing factor to lower than desirable deployment is insufficient staffing.

Figure 1: Historic Loan Activity: FYE 2012 through June 30, 2015

	FYE 2012	FYE 2013	FYE 2014	YTD 2015
Total Loans O/S ($)	$167,567	$190,000	$362,820	$340,919
Total Loans O/S (#)	25	52	67	70
Loans Disbursed ($)	$150,000	$185,090	$280,000	$72,045
Loans Disbursed (#)	12	30	38	16
Deployment(a)	45%	43%	66%	59%

(a) Calculated As Total Loans Outstanding/(Debt + EQ2 +Net Assets Available For Financing)
(b) Data supplied by NACLF.

NACLF has a relatively narrow menu of loan product offerings, several of which contain lender-imposed borrower restrictions. For example, loans funded by the United Way may be used only in a peer lending circle model, while loans funded by the Office of Refugee & Resettlement can only be loaned to a people with refugee status, which changes from time to time depending upon the social, economic and political climate.

LOAN PORTFOLIO PERFORMANCE

As shown in Figure 2 below, the NACLF's portfolio quality is improving, as evidenced by a substantial drop-off both in the percentage of the total portfolio at risk and the annual net loss ratio.

Figure 2: Historic Loan Portfolio Quality

	FYE 2012	FYE 2013	FYE 2014	FY 2015
Total Loans O/S ($)	$167,567	$190,000	$362,820	$340,919
Amount Delinquent	$49,130	$47,472	$40,200	$30,111
Total Portfolio At Risk	29.3%	25.0%	11.1%	8.8%
Total Net Write-Offs	$40,300	$33,468	$25,308	$17,387
Annual Net Loss Ratio	24.1%	17.6%	7.0%	5.1%
Loan Loss Reserve (accrual)	$17,500	$20,660	$36,815	$31,635

Note: Data supplied by NACLF.

CONCLUSION

NACLF has established a market for its loan products and services. Nonetheless, deployment levels are lower than desirable, most likely due to insufficient or irregular staffing or both. The majority (perhaps as high as 100 percent) of the NACLF's loan referrals are through the CDC, and there is excellent synergy between the product and services offerings between the CDFI and its parent organization. However, it appears that the NACLF has not reached out beyond its organizational confines to new, potential partners. As noted in the Organizational Management and Board Governance section, the NACLF Board of Directors needs to establish greater clarity about the staffing and operational commitment of its parent, the CDC. The NACLF's loan practices could also be strengthened, for example, by establishing a cash-funded loan loss reserve; by using a risk rating system to monitor portfolio quality; and, by institutionalizing practices such as regular portfolio reviews. Further, the NACLF must identify new sources of loan capital and operating support if it is to grow the CDFI and develop long-term organizational sustainability.

RESOURCE AND FINANCIAL MANAGEMENT

CAPITALIZATION AND LENDING CAPTITAL

For the most recent fiscal year (December 31, 2014), the NACLF's parent organization (the CDC) showed nearly $4.5 million in consolidated total assets and $3.8 million in total net assets. Of total assets, approximately $558,000 (or, 12.4 percent) pertain to NACLF activities and are comprised exclusively of cash and notes receivables. Assets are supported by approximately $323,000 in liabilities with the balance ($235,000) in total net assets for a 42 percent net worth ratio. At June 30, 2015 total assets had increased to nearly $585,000, with approximately the same amount in total liabilities and net worth as of the last fiscal year-end.

The NACLF has used a combination of borrowed and grant capital to support loan activity. Since inception, it has cultivated a small, concentrated group of investors/funders, as follows:

NACLF Pooled Loan Fund Center City Bank and Fairhaven Bank each provide a line of credit totaling approximately $250,000 which provides the NACLF with funds to support loans to naturalized citizens or refugees in amounts of up to $40,000. As of June 30, 2015, $164,000 of this line was drawn.

United Way provides the NACLF with grant funds to support loans to low income, immigrant women in amounts of up to $1,000 that are used to support very small microenterprises.

Office of Refugee Resettlement (ORR) of the U.S. Department of Health & Human Services provides the CDC with a five-year operating grant; the CDC is entering the final year of the grant. A portion of these funds is passed through to the NACLF, enabling it to make loans to refugees in amounts of up to $15,000. Loans are extended to new or existing microenterprises, and may support working capital, inventory, supplies, furniture, fixtures, machinery, tools, equipment, building renovation, and/or leasehold improvements.

The NACLF also has two small EQ2 investments totaling $150,000 from major national banks that are priced at five percent ($100,000) and four percent ($50,000) respectively. The NACLF does not have an asset-liability matching strategy.

OPERATIONS AND LONG-TERM SUSTAINABILITY

For fiscal year end 2014, NACLF generated approximately $140,000 in total revenue and support. Of this amount, $32,000 (or nearly 23 percent) represented earned income, i.e., fees and interest income derived from lending activities. Total expenses for the same period were nearly $115,000, for a total increase in net assets of nearly $20,000.

It should be noted that the NACLF does not systematically assess interest rate risk. According to a brief discussion found in the June 2015 board minutes, NACLF's interest expense was higher than interest income for first quarter, 2015. While no data was available on the average weighted interest rate generated by the portfolio compared to the average weighted cost of debt, management indicated that the CDFI earns a three percent net interest margin from its bank pooled loan funds and a two percent net interest margin on EQ2 funds.

The ORR funds and the United Way funds are grants, and thus, the cost of these sources of capital is zero. However, the United Way loans are also extended to borrowers with a zero-interest rate, so the NACLF also earns no interest on these funds. The imbalance in interest expense/income is likely due to low loan activity (i.e., NACLF is booking fewer loans); higher-than-average pay-offs (i.e., the loan portfolio is shrinking); and improper pricing.

NACLF is heavily subsidized, primarily through donated staff and administrative/financial services provided on an in-kind basis by its parent organization. To date, NACLF has obtained only limited operational support from external funders. The financial relationship between the two organizations is memorialized in a Memorandum of Understanding that is negotiated yearly. A close review of this three page document, combined with discussions with management, suggests that the NACLF has limited control over its annual budget or programmatic activities.

It is also likely that the operating expenses in the NACLF's budget do not accurately reflect its total cost of operations. Since all employees are CDC employees, and there is no rigorous or true cost allocation between the two organizations, it is difficult (if not impossible) to assess the NACLF's actual cost of operations. Through October 31, 2015, the CDC had provided over $50,000. According to management, without this subsidy, the NACLF would have generated a loss of approximately $2,500 per month.

During the past year, the NACLF's president attended a NeighborWorks® Training Institute class on financial sustainability that resulted in access to, and use of, an Excel-based financial model. Management can use this model to manipulate various inputs (e.g., staffing levels, loan volume, pricing, etc.) and assess the impact on cash flow and net income. This tool will be helpful in better understanding the financial drivers contributing to long-term sustainability.

LIQUIDITY

Liquidity is very strong, in part due to relatively low capital deployment, as well as NACLF's ongoing access to a bank line of credit. NACLF's current ratio was 3.2 (FYE 2012); 25.7 (FYE 2013) and 56.6 (FYE2014). For the period ending December 31, 2014, days of cash on hand was equal to 697 days (or nearly two years).

FINANCIAL REPORTING AND ACCOUNTING PROCEDURES AND PRACTICES

NACLF prepares quarterly financial statements; the annual financial audit is reported on a consolidated basis. The president submits financial reports at each board meeting. These financial statements do not show actual results against budget. NACLF's financial statements are prepared by a CDC employee; it uses the parent organizations' accounting manual.

CONCLUSION

NACLF has limited access to stable, predictable sources of low-interest lending capital. Due to generally low loan volume and the ready availability of a bank line of credit, liquidity levels are very high, but earned income is minimal, contributing to low levels of self-sufficiency. Further, the NACLF lacks sufficient staffing that would be available to (i) identify new sources of lending and operating capital, (ii) consistently undertake marketing and business development and (iii) conduct underwriting new loans. These factors pose serious constraints to future growth and make it difficult to assess the NACLF's long-term sustainability.

ORGANIZATIONAL MANAGEMENT AND BOARD GOVERNANCE

BOARD GOVERNANCE MODEL AND COMMITTEE STRUCTURE

The NACLF is led by a 13-member Board of Directors, although the number of directors is variable due to a steady stream of additions and departures. The NACLF's president serves in an ex-officio member capacity. According to its by-laws, the board has one voting member (i.e., its parent corporation, the CDC) that, in turn, annually elects the Board of Directors at the annual meeting.

The board operates with three formal committees: the executive committee, the nominating and board building committee, and the finance/audit committee, which meet on an as-needed basis. NACLF also operates with a standing loan committee that is comprised of two board members and three bankers from the NACLF loan pool.

PERTINENT SKILLS AND ENGAGEMENT

The board roster indicates that the NACLF is served by individuals with appropriate and useful experience, including attorneys, certified public accountants, bankers (mortgage and commercial) and senior business professionals. Two individuals on the board are engaged in activities that are directly relevant to the NACLF's operation: one is a business development specialist with the Small Business Development Center of State University and another is an accountant with the County Economic Council.

Per the NACLF's by-laws, at least 50 percent of the board is required to consist of representatives of the constituency that the NACLF serves, such as community representatives and/or stakeholders of the ethnic populations and/or low income neighborhoods and communities.

Board meetings are held quarterly, although there is discussion of increasing board meetings to six times per year. According to management, as well as a review of the board minutes for the past 18 months, board attendance is judged to be sporadic. In April, 2014, members of the board participated in a strategic planning meeting.

STAFF CAPACITY

At FYE 2014, the NACLF had a staff of four FTEs; staff is employed by the CDC. At the time of this report, the NACLF's staff was decreased to 2.75 FTEs due to budget cutbacks imposed by the CDC.

The CDC extends staff capacity by using volunteers for providing development services (primarily local bankers who receive CRA credit); CDC employees provide back-office and financial/administrative support, including HR, IT, and accounting. The NACLF's president has a dual responsibility as the CDC's senior vice president for finance and business development. He estimates that 25 percent of his time is spent on NACLF related activities.

According to the NACLF president, the ability to properly and consistently staff the CDFI is an ongoing problem. Issues include: (i) historically high rates of staff turnover, (ii) identifying the right staff sizing/configuration with regard to current and projected loan activity, (iii) finding qualified staff with lending experience, and (iv) budgetary constraints.

CONCLUSION

The NACLF is a relatively young organization. While it has established governance and staffing structure, the organization faces important challenges for securing its long-term sustainability. Perhaps the greatest concern is the NACLF's staffing levels. With the current staffing configuration, it is highly unlikely that the NACLF will be able to grow and thrive organizationally. Moreover, it is doubtful that the NACLF will be able to generate the kind of impact that it is capable of, without a larger, consistent commitment of financial and human resources.

RECOMMENDED ACTION PLAN

The following recommendations are listed by timing i.e., short term (within 12 months), intermediate term (between one and three years), or longer term (more than three years). Within each term category, highest priority recommendations are listed first.

Short Term

- Increase the level of active board participation. Consider a smaller but more engaged board.
- Prepare quarterly financial statements on an actual vs. budgeted basis so that management and the Board of Directors can accurately and regularly assess performance and progress against goals.
- The NACLF and the CDC should further refine the nature of the operating agreement and more clearly assess the NACLF's staffing and administrative needs as well as the CDC's ability to realistically meet those needs.
- Examine the current pricing strategy relative to the cost of funds and net interest margin targets so as to avoid negative arbitrage. The NACLF also may wish to consider paying down high-priced debt, given its high levels of liquidity.

Intermediate Term

- Strengthen lending policies and procedures through adoption of standard practices such as a loan risk rating system, loan charge-off procedures, portfolio risk monitoring and review activities, and loan approval levels.
- Identify and aggressively pursue new sources of operational support. Since the CDC itself is heavily subsidized, downturns in the CDC's funding negatively affect the NACLF.
- Use the financial modeling software provided by the NeighborWorks Training CDC to develop a realistic plan for future sustainability. Key elements of this plan should include identifying possible sources of capital (lending and operating) as well as a reasonable staffing configuration. Management should seek out available sources to develop reasonable peer comparisons (e.g., the Association of Enterprise Organizations, the Opportunity Finance Network).
- The Board of Directors of the NACLF and the CDC must together re-affirm their commitment to the NACLF's long-term sustainability. The NACLF's board should further commit to improving and strengthening staff skills and professional development, especially with regard to CDFI issues, microenterprise lending and financial management.
- Develop a long-term vision and produce a strategic plan, with an emphasis on, and in context with, the relationship with the CDC (i.e., issues such as board representation, mission consistency, financial dependence, long-term sustainability).

- Continue to expand and solidify NACLF market presence by reaching out to new customers and partners beyond those referred through the CDC.

- Develop realistic, achievable and measurable targets for deployment, self-sufficiency and loan fund liquidity.

- Write (or, contract for) a capitalization plan. Such a plan would address how much capital the NACLF needs to raise to support loan growth and reach self-sustainability, as well as identify likely sources of capital. For example, the NACLF should aggressively pursue funding from the SBA Microenterprise Lending Program, which offers both lending and operating capital. The NACLF may also wish to consider faith-based investors, most of which operate with a similar mission and programmatic focus.

- Require bankable borrowers to pay by EFT or another automated method as a means of increasing timely borrower repayment, thus reducing delinquencies.

Long Term

- Establish a cash-funded loan loss reserve. The NACLF's loan loss reserve account is on an accrual basis only, thus funding all losses with its fund balance. A cash-funded loan loss reserve should be a major element as part of the organization's overall loan fund capitalization strategy.

APPENDIX A

OVERVIEW OF LOAN PRODUCTS

CDC Pooled Loan Fund Loans: In partnership with four commercial banks, NACLF makes microloans from the NACLF pooled loan fund.

General Eligibility:

- Can be a naturalized citizen or refugee

Benefits:

- Application assistance
- Fixed interest rate is 3 points above prime but not lower than 7%
- Flexible credit requirements
- Loans for start-ups and existing businesses
- Assistance before and after loan is made

Terms:

- Maximum loan of $40,000
- Maximum maturity of 5 years
- Secured with collateral or cosigner

Requirements:

- Minimum 20% investment from borrower
- $25 application fee
- Closing costs based on size of loan (up to $200)

Peer Lending Circle: The Peer Lending Loan Fund began in 2011 with funding from a special initiative from the United Way for "Micro-Lending & Microenterprise Development for Low-Income Women."

General Eligibility:

- Low-income immigrant women

Benefits:

- Group meets regularly, creating incentive and support for members
- New members receive loans as old members repay
- Assistance from staff before and after loan is made

Terms:

- Maximum loan of $1,000
- Maximum maturity of 18 months
- Zero interest

Office of Refugee Resettlement Loans: Funding for loans to refugee entrepreneurs comes from the Office of Refugee Resettlement of the US Department of Health & Human Services.

General Eligibility:

▪ Must be a refugee (not yet a citizen)

Benefits:

▪ Application assistance

▪ Fixed interest rate tied to prime

▪ Flexible credit history requirements

▪ Loans for business start-ups and existing businesses

▪ Assistance before and after loan is made

Terms:

▪ Maximum loan of $15,000

▪ Must be repaid in 3 years or less

▪ Secured with collateral or cosigner

Requirements:

▪ Minimum 20% investment from borrower

▪ $25 application fee

▪ Closing costs based on size of loan (up to $200)

APPENDIX B

SUMMARY OF KEY FINANCIAL DATA, 2012-2015

(All data removed from this chart to maintain anonymity of the CDFI.)

SUMMARY TABLE	FYE 2012	FYE 2013	FYE 2014	FY 2015
Assets				
Current Assets				
Cash & Cash Equivalents				
Notes Receivable				
Total Assets				
Capital				
Total Assets				
Unrestricted Net Assets				
Temporarily Restricted Net Assets				
Total Net Assets				
Net Worth Ratios				
Net Assets/Total Assets				
Unrestricted Net Assets/Total Assets				
Net Assets & EQ2/Total Assets				
EQ2 & Debt				
EQ2				
Current Liabilities (ST Notes & AP)				
Senior Debt				
Total Debt				
Debt Ratios				
Senior Debt/Total Assets				
Total Debt/Total Assets				
Leverage				
Total Debt/Net Assets				
Asset Quality				
Total Outstanding Loan Portfolio				
Loan Loss Reserve (non-cash)				

SUMMARY TABLE	FYE 2012	FYE 2013	FYE 2014	FY 2015
Delinquency (>90 days)				
Delinquency (>90 days)/Outstandings				
Annual Write-Offs				
Loan Loss Reserve/Outstandings				
Gross Amount Charged Off/Outstandings				
Earnings				
Earned Revenue				
Grant Revenue				
Operating Expenses				
Financing Expenses				
Total Expenses				
Surplus from Operations				
Net Margin				
Self Sufficiency				
Earned Revenue/Total Operating Expenses				
Liquidity				
Cash & Cash Equivalents/Current Liabilities				
Current Assets/Current Liabilities				