A CDFI, the CRA, and the RS Fiber Cooperative

OFN Webinar
Thursday, June 22, 2017
Speakers

• Linda Salmonson, Economic Development Manager, Rural Electric Economic Development, Inc.
• Mark Erickson, Economic Development Director, City of Winthrop, Minnesota
• Tim Herwig, District Community Affairs Officer, Office of the Comptroller of the Currency
Rural Fiber Optic Infrastructure

How can CDFIs (and Banks) finance innovative economic development efforts that revolutionize opportunity in rural communities?
RS Fiber Cooperative

• RS Fiber Cooperative is a community driven effort to bring high-speed fiber optic connectivity to the people, businesses, schools, hospitals/clinics, and government agencies of 10 communities and 17 townships in Renville, Sibley, and portions of Nicollet and McLeod counties in southwestern Minnesota.

• The RS Fiber telecommunications network will serve more than 6,000 households, farms, and other businesses in a 700+ square-mile area with both wireless and universal fiber-optic service.

• Construction will cost an estimated $45 million

• RS Fiber provides direct fiber optic connectivity at up to 1 gigabit of bandwidth at prices significantly reduced from current commercial providers. This fiber to the home service (FTTH) has become the leading technology for next-generation communications worldwide.
Rural Electric Economic Development

- Rural Electric Economic Development (REED) provides business and community project financing in partnership with commercial and other economic development lenders to leverage private investment in the region it serves.
- Governed by 22 electric cooperatives in 50 counties in eastern South Dakota and western Minnesota, REED assists projects that promote growth and contribute to job, business and wealth creation, as well as improve the infrastructure, community facilities/services and economic base of rural areas.
Office of the Comptroller of the Currency

- The OCC charters, regulates, and supervises national banks, federal savings associations, and federal branches and agencies of foreign banks. The OCC is an independent bureau of the U.S. Department of the Treasury.
- The OCC’s mission is to ensure that national banks and federal savings associations operate in a safe and sound manner, provide fair access to financial services, treat customers fairly, and comply with applicable laws and regulations.
- Community Affairs supports the mission by helping national banks and federal savings associations provide safe and sound community development financing and making financial services accessible to underserved communities and consumers. Community Affairs does so by serving bank examiners, banks/thrifts, and communities through consultations, outreach, and publications.
The Community Reinvestment Act

- The Community Reinvestment Act encourages depository institutions to meet the credit needs of low- and moderate-income (LMI) individuals and communities
- Passed to address discrimination in access to loans and credit
- Requires agencies to evaluate the performance of banks in meeting the credit needs in the communities in which they are chartered.
- Passed in 1977–has been revised since then
What Gave Rise to the CRA?

• A result of community struggle and activism
• Part of the neighborhood movement of 1970s-80s
• A campaign against deteriorating conditions in urban, lower-income neighborhoods, related to:
  – Redlining
  – Disinvestment
  – Housing discrimination
Purpose of the CRA

• Encourages federally insured banks and thrifts to help meet the credit needs of their entire communities, in particular, historically underserved people and places (this may include working together with community organizations to promote the availability of credit and other banking services)
  – Low- and moderate-income people
  – Low- and moderate-income geographies
  – Underserved or distressed non-metropolitan middle-income geographies, or certain designated disaster areas
  – Must be consistent with prudent, safe, and sound business operations
Purpose of the CRA (cont.)

- The CRA requires regulators of federal depository institutions to assess the record of each bank and thrift in helping to fulfill their obligations to the community and to consider that record in evaluating applications for charters or for the approval of bank mergers, acquisitions, and branch openings.
  
  - An affirmative obligation
  - Rating of Outstanding, Satisfactory, Needs to Improve, or Substantial Noncompliance
  - Interpreted through implementing regulations and guidance
  - Enforcement primarily through corporate application process and reputation risk
  - CRA contains no civil or criminal liability provisions
Q&A § 12(g)(4)(iii) New Example - Activity in Underserved Nonmetro Middle-Income Geo

- Provides guidance on how examiners consider activities related to the expansion of broadband infrastructure in CRA defined underserved non-metropolitan middle-income geographies
  - Important to global competitiveness, job creation, innovation, and expansion of markets for American businesses
- Availability of broadband is essential to:
  - Access digital banking services, particularly in light of shift away from branch-based delivery systems
  - Promote economic development as small businesses become more reliant on related technologies for payment processing systems, remote deposit capture, access to credit facilities and markets, and to deliver products
Public Welfare Investment Authority (PWI)

- OCC’s public welfare investment (PWI) authority is one tool for a national bank to help meet the credit needs of its communities.
- National banks may make investments, directly or indirectly, that are primarily designed to promote the public welfare such as by providing housing, services, or jobs, under the investment authority in 12 USC 24 (Eleventh) and the implementing regulation, 12 CFR 24.
- By “investments,” we mean both equity investments and debt investments, such as equity equivalent investments or other debt.
- By “public welfare investment,” we mean investments that primarily benefit low- and moderate-income individuals, low- and moderate-income areas, or other areas targeted by a government entity for redevelopment, or if the investments would receive consideration under 12 CFR 25.23 (the Community Reinvestment Act regulation) as a "qualified investment."
PWI (cont.)

• National bank PWI examples:
  – Support for affordable housing and other real estate development
  – Equity for start-up and expansion of small businesses
  – Investments in CDFIs
  – Activities that help to revitalize or stabilizing a government-designated area.

• Other financial institutions follow different PWI rules:
  – Federal savings associations are supervised by OCC. However, they follow statutory and regulatory authorities that are different than for national banks.
  – Non-member state banks are supervised by the Federal Deposit Insurance Corporation.
  – Member state banks and holding companies are supervised by the Federal Reserve System.

• Financial institutions should consult with their respective regulators about whether a PWI would be considered consistent with their respective investment authorities.
PWI Requirements: Primary Purpose

- A national bank’s PWI must primarily benefit at least one of the following (12 CFR 24.3)
  - Low- and moderate-income individuals
  - Low- and moderate-income areas
  - Areas targeted by a government entity for redevelopment
  - The investment would receive consideration under 12 CFR 25.23 (the Community Reinvestment Act regulation) as a "qualified investment."
PWI Requirements: Investment Limits

• Limits on Aggregate Outstanding Investments - 12 CFR 24.4(a)
  – Aggregate investments may reach 5 percent of a bank’s capital and surplus
  – With prior approval, aggregate investments may go up to 15 percent of a bank’s capital and surplus

• Limited Liability – 12 CFR 24.4(b)
  – Investments must be structured to not expose the bank to unlimited liability
PWI Requirements: Record-keeping

- A national bank making a public welfare investment under 12 CFR 24 shall maintain in its files information adequate to demonstrate that its investments meet the public welfare beneficiary standards and investment limit requirements. (12 CFR 24.7(b))
PWI & R/S Fiber Optic

- A national bank operating in the R/S Fiber Optic Cooperative’s proposed service area recently requested and was granted permission by the OCC to purchase stock shares in the cooperative under the public welfare investment authority.
- The cooperative was organized to bring high-speed fiber optic connectivity to communities in west central Minnesota and provide broadband service to homes, farms, businesses, health care facilities, schools, and local government offices at prices significantly reduced from current commercial providers.
- Project would result in enhanced economic development opportunities for businesses and job creation for local residents.
How R/S Fiber Optic Met PWI Requirements

• Primary Purpose: Bank demonstrated that the investment will primarily benefit low- and moderate-income individuals, low- and moderate-income areas, and other areas targeted by a government entity for redevelopment
  – Project services census tracts that are moderate-income or in distressed non-metropolitan middle-income census tracts
  – Project creates permanent jobs that will be pay salaries that fall within the range of 80 percent of area median income of the targeted counties
  – Project receives financial support from government entities, including a grant from the state, loan from economic development authorities, and local tax abatement bonds

• Investment limits:
  – Bank’s investment was less than 1 percent of its capital and surplus
  – Bank’s purpose of preferred stock would not expose it to unlimited liability
  – No safety or soundness concerns regarding bank’s investment
PWI Requirements: Fiber Optic Investment Activities

- Part 24 contains examples of Qualifying PWI Activities (12 CFR 24.6)
- Fiber optic projects generally consistent with economic development examples 12 CFR 24.6(b)
  - Investment that provides financing for a small business or farm located in a LMI area
  - Investment that provides financing for a small business or farm that produces or retains permanent jobs, the majority of which are held by LMI persons
  - Investment that develops and operates a commercial or industrial property located in a LMI area or that is occupied by a small business that produces jobs for LMI persons
  - Investment that develops and operates a business incubator located in a LMI area or that is occupied by a small business that produces jobs for LMI persons
  - Investment that forms and operates an agricultural cooperative located in a LMI area or that produces jobs for LMI persons
- Fiber optic investments are novel PWIs. Recommend that banks should seek prior approval before proceeding
Non-MSA Low- and Moderate-Income and Distressed and Underserved Census Tracts

- Part 24 contains examples of Qualifying PWI Activities (12 CFR 24.6)
- Fiber optic projects generally consistent with economic development examples (12 CFR 24.6(b))
- Investment that provides financing for a small business or farm located in a LMI area
- Investment that provides financing for a small business or farm that produces or retains permanent jobs, the majority of which are held by LMI persons
- Investment that develops and operates a commercial or industrial property located in a LMI area or that is occupied by a small business that produces jobs for LMI persons
- Investment that develops and operates a business incubator located in a LMI area or that is occupied by a small business that produces jobs for LMI persons
- Investment that forms and operates an agricultural cooperative located in a LMI area or that produces jobs for LMI persons

Fiber optic investments are novel PWIs. Recommend that banks should seek prior approval before proceeding.
FCC 25 Mbps Broadband Deployment
Locating LMI, Distressed and Underserved Non-Metropolitan Middle Income Census Tracts

    - Census Demographic Data by County
    - Census Demographic and other Data by Census Tract
  - Distressed and Underserved Tracts: [http://www.ffiec.gov/cra/distressed.htm](http://www.ffiec.gov/cra/distressed.htm)
Locating Regulated Financial Institutions by County and MSA

- FDIC Summary of Deposits Website: [https://www5.fdic.gov/sod/](https://www5.fdic.gov/sod/)
  - Individual Counties/MSAs
  - Aggregated Counties (up to 10)
  - Financial Institutions
    - Deposits within and without county or MSA
    - Branches: Deposits
    - CRA Evaluations
    - FFIEC Uniform Bank Performance Report (UBPR)
      » Bank’s Balance Sheet
Contact Information

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RS Fiber Footprint today

Footprint located an hour West/Southwest of Twin Cities
History of RS Fiber

What is RS Fiber?

$55 million 308B telecommunications cooperative covering parts of Sibley and Renville Counties in Minnesota.

Public/Private Partnership model includes 10 rural communities - smallest is 400 and largest 2,300 in size.

Also includes 17 townships as Phase 2 financing partners for fiber-to-the-farm.

Symmetrical gigabit capable active Ethernet network.

Phone, cable TV and Internet service
  - Capable of 4K television viewing

Phase 1 is fiber to cities with wireless to farms.

Phase 2 will replace wireless with fiber to the farm within seven year.
How We Got Started

Started in 2010 with a feasibility study that showed a fiber business could be profitable with enough customers - including bringing fiber to the farms - and the right financing package.

Grassroots education critical to the process

- 150+ local meetings
- 14,000 fiber primers mailed
- Door-to-door pledge drive
- Newspaper ads
- Billboards
Getting Ready to Obtain Financing

- Created a Joint Board made up of cities and counties.
- Created ‘shovel ready’ package
  - Local volunteers - obtained 56% pledge card to prove demand
  - Local bank consortium
- David Drown Associates - local bond advisor
- Hiawatha Broadband - overall operator of the system
- CCG Consulting - financial models
- Finley Engineering - engineering
First Attempt to Get Financed

- Tried to finance with 100% revenue bonds
- Bond issue proved to be impractical
  - Bond attorneys for different parties couldn’t agree on all issues
  - More importantly, size of the borrowing exceeded the borrowing capacity of some of the cities
- For a while it looked like the project was dead
- David Drown Associates proposed an alternate model with a Public Private Partnership that includes the 10 cities and 17 townships in collaboration with the newly formed RS Fiber Cooperative
Public Private Partnership Model

- Support from local ag producers was critical to start up as well as support from area farm ag cooperatives.
- The project was funded with a mix of financing that includes G.O. Tax Abatement bond proceeds from the cities that were loaned to the cooperative.
- Added mix of $1 million from state broadband grant, $6 million from local bank consortium, member equity, REDL & G and REED programs.
- Cooperative makes the bond payments on behalf of the cities. 20-year term at about 4%. Taxable bond.
## City contribution to financing (Phase 1)

<table>
<thead>
<tr>
<th>Cities</th>
<th>2010 Households</th>
<th>% of Total</th>
<th>Debt Allocation</th>
</tr>
</thead>
<tbody>
<tr>
<td>Fairfax</td>
<td>577</td>
<td>7.95%</td>
<td>$1,191,984.58</td>
</tr>
<tr>
<td>Gibbon</td>
<td>394</td>
<td>5.43%</td>
<td>813,937.47</td>
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<tr>
<td>Winthrop</td>
<td>640</td>
<td>8.81%</td>
<td>1,322,131.94</td>
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<tr>
<td>Gaylord</td>
<td>996</td>
<td>13.72%</td>
<td>2,057,567.83</td>
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<tr>
<td>New Auburn</td>
<td>206</td>
<td>2.84%</td>
<td>425,561.22</td>
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<tr>
<td>Green Isle</td>
<td>240</td>
<td>3.31%</td>
<td>495,799.48</td>
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<tr>
<td>Lafayette</td>
<td>244</td>
<td>3.36%</td>
<td>504,062.80</td>
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<tr>
<td>Buffalo Lake</td>
<td>327</td>
<td>4.50%</td>
<td>675,526.79</td>
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<tr>
<td>Stewart</td>
<td>261</td>
<td>3.59%</td>
<td>539,181.93</td>
</tr>
<tr>
<td>Brownton</td>
<td>349</td>
<td>4.81%</td>
<td>720,975.07</td>
</tr>
<tr>
<td><strong>10 Cities</strong></td>
<td><strong>4,234</strong></td>
<td><strong>$</strong></td>
<td><strong>8,746,729.10</strong></td>
</tr>
</tbody>
</table>
Where is RS Fiber Today?

First two years of construction:
- 100 mile fiber backbone connecting 10 cities
- Six cities fully built out
- 13 wireless towers are active and attached to fiber backbone
- 1,300 customers and counting, including 500+ ag producers.
- Adding approximately 100 customer per month.

Four remaining towns operational by end of 2017

Also constructing fiber backbone through all of Renville County for possible Phase 3 construction to more communities and farms.
Not Just a Fiber Network

- Opened Innovation Center and Digital Literacy Learning Center via three-year collaboration with University of Minnesota Extension Service. Includes:
  - STEAM curriculum offered through 4-H and area schools.
  - Broadcast technology curriculum will teach students and adults to write, direct and produce their own videos.
  - Plans are to continue to use the network to improve education, health care and agriculture opportunities for everyone in the area.
What have we learned from RS Fiber?

- Don’t give up if business plan and area support are positive.
- Local community support and involvement is important.
- A local champion is essential.
- It will take more time and effort than you expect.
- It takes a team (consulting, legal, banking, operational, engineering, construction) working together.
- Be creative with financing - it’s nearly impossible to finance a new fiber start-up from only one financing source.
- Not necessary to bring fiber everywhere on day one as long as there is a long-term plan.
- Phone and cable companies are unable to make the necessary investment. If cities/townships want fiber access they are going to have to make it happen themselves.
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RURAL ELECTRIC ECONOMIC DEVELOPMENT (REED) FUND

Nonprofit CDFI

Serves 45,000 square miles of rural SD and MN

$49 million capital

Community and business lender
R-S FIBER COOPERATIVE

Financial Issues

- Large scale project
- Unserved or underserved region
- Committed towns and townships
- Fiscal leadership and cooperative support
- Strategic partners
- It’s a complicated start-up
RS Fiber Cooperative

CCG Consulting

Hiawatha Broadband

Sterling Capital Advisors

Senior Lenders

ProGrowth Bank
- Notes B,C,D, and E
- 6 Private Investors
- ProGrowth Bank
- Note A
- 2 Community Banks
- ProGrowth Bank
- Note G
- REED
- Note G
- R-S Electric Cooperative
- USDA REELG Loan – Note F

Subord. Investors
- Joint Powers Board G.O. Loan $8.677 MM
- New Market Tax Credits (7 years)
- HUD Section 108 Loan (Future)

Equity Investors
- Patron Members
- Non-Patron Investors
- FNB Fairfax $50K Investment
- State of MN Broadband Grant $1MM

Net Income
R-S FIBER COOPERATIVE

Lessons Learned

- Broadband is an essential community service
- Lack of access impacts business and quality of life
- There are lots of financing dead ends
- It is a hybrid system
- The region needs a backbone system
- Local telephone providers aren’t taking the risk
- Without the fiber ring, high speed is not possible
- Federal programs are geared toward the last mile, service such as education and telemedicine
Questions?

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