Office of Thrift Supervision

Best Practices in Rural Development

including
Agriculture Information
Bulletin Number 710
"**Understanding Rural America**"

Community Affairs

Acknowledgment

The Office of Thrift Supervision gratefully acknowledges the efforts of Kevin J. Davis, a Community Development specialist who has served in the OTS Fellowship Program since July 1997, in the preparation of this paper, "*Best Practices In Rural Development*". Much of this paper was prepared by Mr. Davis following his year long effort to research and locate the twelve diverse rural development programs featured as Best Practices and interview those individuals who are primarily responsible for the success of each of these programs. The Office of Thrift Supervision also appreciates the cooperation of the staff of the United States Department of Agriculture who, among other things, permitted the use of Agriculture Information Bulletin No. 710 "*Understanding Rural America*" to provide this paper with a comprehensive overview of rural America.

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Introduction

As the regulator of a large number of financial institutions that are located in rural areas, the **Office of Thrift Supervision** ("OTS") has a particular interest in improving the economic outlook of rural communities. That interest is grounded in the belief that efforts expended toward such improvement are not only socially desirable but also can represent sound business decisions when they improve the economic prospects of the markets in which the financial institutions operate. For these reasons, the OTS has endeavored to identify programs and initiatives designed to provide capital and credit to rural areas. Our findings are presented in the following paper entitled "***Best Practices in Rural Development***."

Recent U.S. Department of Agriculture ("USDA") studies indicate that rural America contains 83 percent of the nation's land and is home to 51 million people, or about 21 percent of the total population of the United States. In its publication titled "***Understanding Rural America***," the USDA points out that the economic well-being of this significant segment of America's population depends upon many things including the availability of good-paying jobs; access to critical services such as education, health care, and communication; strong communities; and a healthy natural environment.

In reviewing the "Best Practices" it is important not to lose sight of the fact that rural America is diverse and, although there are similarities between rural regions there are also profound differences. No single economic diagnosis or prescription fits all. For example, the problems and solutions in Appalachia can be quite different from those in the farm belt of the central U.S. In order to best describe the composition and needs of the various rural regions, we have relied on the experts and have included herein the USDA publication "***Understanding Rural America***" as a critical backdrop for the "Best Practice" discussions.

Although much progress has been made in improving the infrastructure of rural America, many parts of the country continue to find it difficult to attract the capital investments needed to upgrade housing, create jobs and improve the overall standard of living. Often, in isolated rural communities, a local financial institution can be one of the most important factors in a community's economic well being.

Thrifts, by virtue of their broad regulatory and statutory authority, are able to fill the diverse needs of a given area. Traditionally, of course, thrifts have been residential mortgage lenders and they have no statutory limit on the amount of residential loans that can be made. Often thrifts will portfolio their mortgage loans rather than selling them to an investor. This can be a major benefit in rural communities where each property is often unique and may be difficult to qualify for the secondary market.

In addition to residential mortgage loans, thrifts can also make nonresidential real estate loans, commercial loans for businesses including farm equipment loans, and a variety of consumer loans including education loans, car loans and credit card loans. Thrifts also have wide authority to make investments that will benefit their communities. For example, recently the OTS issued legal opinions concluding that a federal association has the incidental authority to (1) make equity investments pursuant to Section 5(c)(3)(A) of HOLA that further community development;[1] (2) invest in Low-Income Housing Tax Credit partnerships;[2] and (3) invest in Farmer Mac common stock.[3]

Although sharing many similarities, all financial institutions are not alike. Differences exist in the statutes and regulations governing the various types of financial institutions; the specific investment authorities and percentage limitations applicable to each institution; the experience and expertise of officers and employees; and the procedures under which investments and loans are made. However, despite these differences, the demographics, economy and needs of a community are the same for each type of financial institution located in that community.

Although the OTS regulates only the thrift industry, financial institutions of all kinds are facing the challenges of being responsive to the needs of their rural communities while maintaining profitability. Consequently, this study focuses on a variety of investments by different types of financial institutions to demonstrate various ways in which a community's needs have been met. By doing so, we hope to provide a broad array of ideas that can then e adapted by any institution to accommodate its particular differences.

Rural communities present unique challenges for financial institutions because of their demographics and needs. In rural communities, a financial institution may be called upon to support any number of community or individual initiatives. In addition to providing loans and investments, managers at rural thrifts are often called upon to provide financial guidance and leadership within their communities. While this is certainly true in urban centers also, in rural areas there are often only one or two financial institutions serving a market. This means that individual financial institutions may exert tremendous influence over their rural communities.

There are three purposes for this study: first, to identify financial institutions in various regions of the country that have implemented innovative programs designed to address problems in their markets and, as a result, have made a positive contribution to their communities; second, to review various government and non-profit initiatives, particularly those that partner with financial institutions and offer assistance in finding solutions; and, third, to acquaint other financial institutions with what can be done, in the hope that they may learn about programs that may fit the needs of their communities.

As with any review of a topic as multi-faceted as the economic development of rural America, the twelve examples contained in this paper are by no means a complete exposition of all the programs nationwide that have been undertaken or that are available. Rather, the “Best Practices” represent those initiatives that have been brought to our attention and that may have broad applicability. In selecting these examples the OTS attempted to present a cross section of geographic locations and organization sizes. We also selected some long standing programs and some that were in the start up phase, as well as some large programs and others that were more modest. The descriptions are necessarily brief and do not contain the myriad of details that would be necessary to implement similar programs. For that reason we have included in each “Best Practice” review the telephone number of at least one contact person who has graciously agreed to provide additional information and assistance.

The “Best Practices” section may be divided into two broad categories of rural development, housing and economic. The first seven “Best Practices” focus on innovative models that have enhanced housing opportunities for their respective communities, including single- and multi-family residential units, loans to finance rehabilitation of housing and a variety of technical assistance. The last five “Best Practices” feature models that have addressed critical economic issues and developed successful vehicles that have enhanced economic growth for the entire community, including small business, agricultural and municipal lending programs.

The 12 “Best Practice” sections that follow the USDA’s publication each contain additional information sources that you may wish to consult. The final sections of this paper include a directory that lists many public and private entities that have been involved in national, regional or local rural development and a list of additional paper and video references.

Finally, it should be noted that the development of programs and initiatives to address the problems of rural America is a dynamic process. This paper is the OTS’ first attempt to set forth some of the practices that we have observed. We know there are many others throughout the country that are not mentioned here and even more in the planning stages. The problems in rural America are likely to receive a much greater degree of attention in the future because of events that could reverse the last century’s urbanization trend in the United States. Among the more notable events are the growing number of stressed-out urban residents who are moving to rural areas for a change of life style; and, the technological changes in the conduct of business, such as telecommuting, that make it less critical to be located in large urban areas. This is an exciting time for rural America and the financial institutions doing business there. Challenges and opportunities abound and we would urge financial institutions, particularly those in rural areas, to develop and/or participate in programs that improve the economic prospects of your communities. We hope you will find some inspiration for doing just that in the following pages.

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[1] CEO Letter 41 (May 31, 1995) summarizing and providing a copy of a May 10, 1995 OTS Chief Counsel opinion.

[2] OTS Chief Counsel Opinion 94/CC-23 (November 10, 1994).

[3] OTS Chief Counsel Opinion P97-11 (October 14, 1997).

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Understanding Rural America

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Understanding Rural America

Economic Research Service
United States Department of Agriculture
Agriculture Information Bulletin No. 710

Washington, DC February 1995

Preface

It has been said that today's decisions determine tomorrow's destiny. Indeed, rural residents and policymakers face many decisions that will affect, if not determine, rural America's destiny. "What are the economic conditions-needs, opportunities, and possibilities-in different rural areas?" "What factors underlie those conditions?" And, ultimately: "How can rural areas and people achieve the goals they aspire to?"

It follows then, that the answers to these and other critical questions should be based on the most accurate, up-to-date information available. Good decisions require good input.

This report draws upon the work of the Rural Economy Division of the Economic Research Service to provide that information. It pulls together the findings of several researchers to describe general rural conditions and trends, as well as details about the many differences found in rural America. The result, we hope, is a source of information that will assist rural decisionmakers as they seek to improve the well-being of rural people and places. ■

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■Notes

The maps and charts in this report are the products of analyses conducted by the Economic Research Service, U.S. Department of Agriculture. Data used in the analyses were provided by the Bureau of the Census, the Bureau of Economic Analysis, and the Bureau of Labor Statistics.

Charts containing the note "1979=100" were indexed to allow for comparison of growth rates. In those charts, the 1979 value of all charted variables was made to equal 100. Thus, values over 100 in subsequent years indicate growth relative to 1979, while values below 100 indicate decline.

Notes referred to by numbers in the text are found at the end of the report.

Introduction

The well-being of America's rural people and places depends upon many things -- the availability of good-paying jobs; access to critical services such as education, health care, and communication; strong communities; and a healthy natural environment to name a few. And while urban America is equally dependent upon these things, the challenges to well-being look very different in rural areas than in urban. Small-scale, low-density settlement patterns make it more costly for communities and businesses to provide critical services. Declining jobs and income in the natural resource -- based industries that many rural areas depend on force workers in those industries to find new ways to make a living. Often those new ways are found only in the city. Low-skill, low-wage rural manufacturing industries must find new ways to challenge the increasing number of foreign competitors. Distance and remoteness impede many rural areas from being connected to the urban centers of economic activity. Finally, changes n the availability and use of natural resources located in rural areas affect the people who earn a living from those resources, as well as those who derive recreational and other benefits from them.

Some rural areas have met these challenges successfully, achieved some level of prosperity, and are ready for the challenges of the future. Other rural areas have met these challenges, but have little capacity to adapt further. Still other rural areas have neither met the current challenges nor positioned themselves for the future. Thus, concern for rural America, its conditions and its future, is real. And, while rural America is a producer of critical goods and services, the concerns go beyond economics. Rural America is also home to a fifth of the Nation's people, keeper of natural amenities and national treasures, and safeguard of a unique part of American culture, tradition, and history.

Translating concern into effective policy for the betterment of rural America is, however, no easy task. The challenge lies, at least partly, in the complex nature of the subject. Rural America, like the rest of America, is changing. Similarly, rural America, like the rest of America, is diverse. These are simple, if not obvious, facts. Yet, in the course of policy debate and formulation, those simple, obvious facts often get lost. In matters of policy, it is tempting to think of rural America as unchanging and homogeneous, to think of it as it once was or as it is now in only some places.

This report aims to provide objective information about the changes taking place in and the diversity of rural America. Toward that end, the report looks at change and diversity from several angles -- its people and places, its economies and industries, its concerns and future. The report begins by examining shifts in rural employment, population, and well-being, continues by analyzing six "county types," and concludes by outlining key realities that effective rural policy will need to recognize.

As with all generalizations, even the disaggregated analysis that follows cannot capture every detail and individual difference. Still, it yields useful information for understanding the complexity of rural America's conditions, trends, needs, and prospects. ■

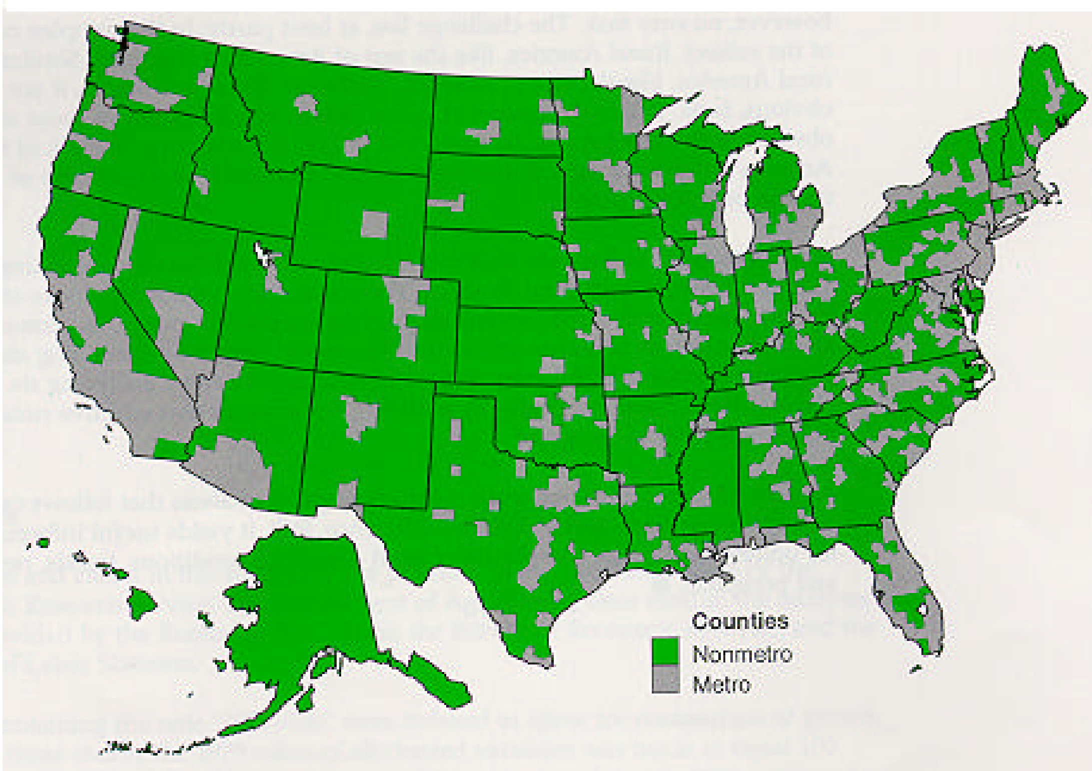
Rural America

A VITAL and CHANGING part of the Nation.

Rural America has been and continues to be a vital part of the Nation. Today, rural America comprises 2,288 counties.[1] It contains 83 percent of the Nation's land and is home to 21 percent (51 million) of its people. In 1992, nonmetro counties supplied 18 percent of the Nation's jobs and generated 14 percent of its earnings. Rural people and communities today are engaged in and depend upon a wide range of economic activities -- from manufacturing to mining, from recreational services to agriculture and everything in between. Yet, rural residents are likely to have many of their needs -- shopping, medical care, banking -- at least partially met by providers in urban areas. This picture of rural America is very different from what it once was.

At the beginning of the 20th century, rural America was the center of American life. It was home to most of the population and was the source of food and fiber for the Nation's

In 1993, nonmetro America accounted for 83 percent of the Nation's land and 21 percent of its population.



sustenance and commerce. And most of its people were involved in producing that food and fiber. The typical rural community in 1900 consisted of a small town or village with numerous small farms within a few miles. Most people lived their lives and fulfilled most of their needs, economic and otherwise, within this community. They had little contact with areas beyond the community.

Rural America has changed in many ways over the century. The rural economy in particular has changed-shifting from a dependence on farming, forestry, and mining to a striking diversity of economic activity. Another significant change has been in the connection between rural areas and cities. Improvements in communication and transportation between the two have reduced rural isolation and removed many of the cultural differences between them. Television, phone service, and transportation systems have helped bring rural and urban dwellers much closer together in terms of culture, information, and lifestyles.

As these changes took place, rural America became home to a smaller and smaller share of the Nation's population. And while it continues to provide most of the Nation's food and fiber, rural America has taken on additional roles, providing labor for industry, land for urban and suburban expansion, sites for storage of waste and hazardous activities, and natural settings for recreation and enjoyment.

And the changes in rural America continue. Following is an examination of some of these key changes. ■

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USDA

USDA

Rural Employment

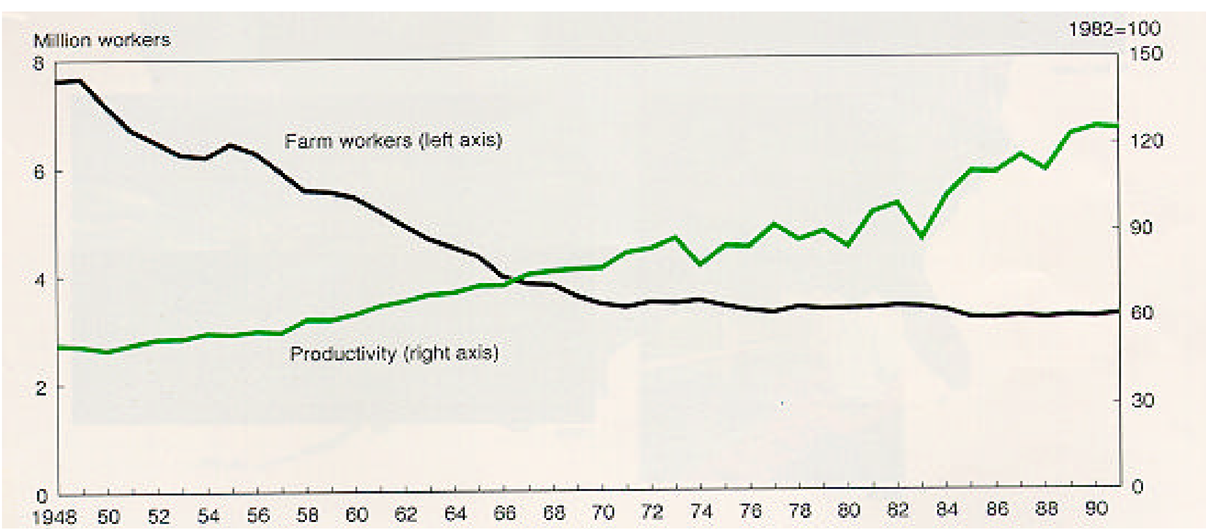
Shifting from farming to manufacturing and services.

In the not too distant past, farming was nearly synonymous with "rural." That is no longer the case. While farming remains important as a source of jobs and income in many rural areas and is the largest single user of rural land, it is no longer the dominant rural industry it once was, nor will it likely be again.

In the last four decades, farming employment dropped from just under 8 million to a little over 3 million. The number of farms has gone from 5.8 million to 2.1 million. In the last 20 years, the percentage of the rural workforce employed in farming has gone from 14.4 percent to 7.6 percent. Even by including agricultural services, forestry, and fishing, the share has gone from only 15.3 percent to 8.5 percent.

Today, only about 5 million people, less than 10 percent of the rural population, live on farms. In addition, in 1990, 58 percent of U.S. farm operator households received wages and salary (averaging nearly $30,000 per reporting household) from off-farm employment. For example, one or more household members might work at a manufacturing plant, telemarketing office, or in retail trade. Therefore, even for the remaining farm households, the nonfarm rural economy is a critical source of employment and income.

Farming's "double-edged sword": increases in productivity mean fewer workers are needed



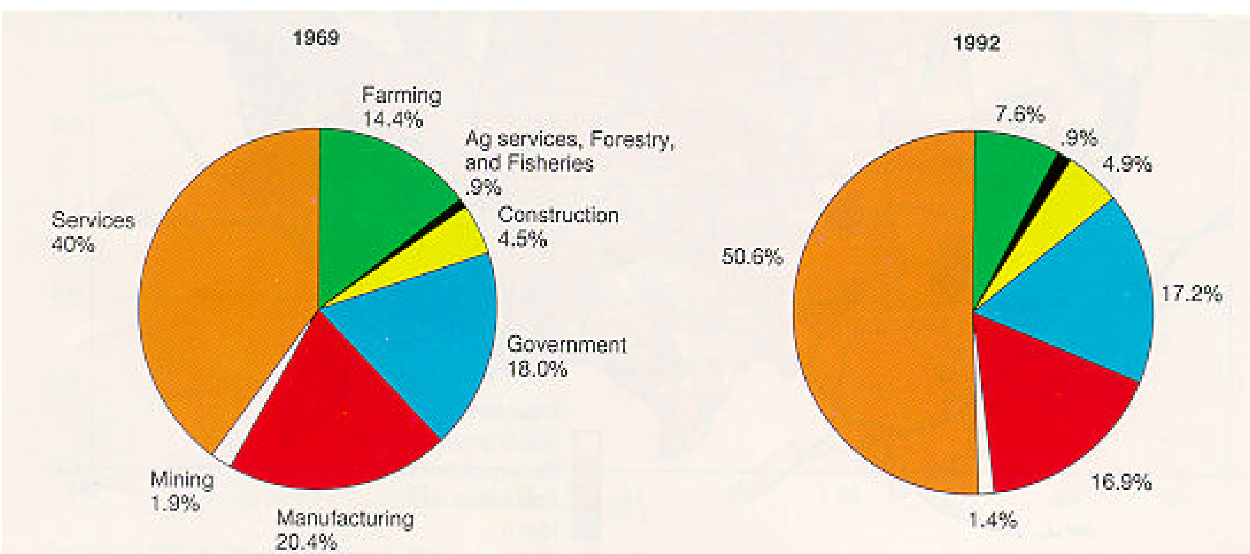
The decline of farming employment is, in many ways, a consequence of success. Improvements in technology, crop science, and farm management have all boosted output while reducing the need for labor. Productivity growth has, in turn, led to farm consolidation, declining farm numbers, decreases in farm employment, and consequently a surplus of farm labor. Thus, the ability to produce more with less, while benefiting many, has caused economic hardship for others.

Today, the largest share of rural jobs and employment growth comes from the services sector, which employs over half of all rural workers. This dominance of the services sector mirrors the urban employment picture. Rural services related to recreation, retirement, and such natural amenities as mountains, lakes, shorelines, etc., have emerged as important new sources of rural employment and growth. Other services -- financial, insurance, real estate, as well as retail stores, dry cleaners, restaurants, etc. -- are also important. And there is anecdotal evidence that advances in telecommunications are enabling still other types of services -- telemarketing, data processing -- to move to rural areas.

Manufacturing also is a major provider of both rural jobs and income, providing jobs for nearly 17 percent of the rural workforce and employing more people than farming, agricultural services, forestry, fishing, and mining combined. Manufacturing also provides roughly a quarter of all rural earnings. However, like farming, the share of manufacturing jobs in rural areas has declined. From 1969 to 1992, that share dropped from 20.4 percent to 16.9 percent of rural employment.

Given these changes in the rural economy, and its current structure, the economic future and well-being of most rural people now depend on the availability and quality of jobs in the rural services and manufacturing sectors and the entrepreneurial opportunities in those sectors.■

Services and manufacturing together employ more than 2 out of 3 rural workers.



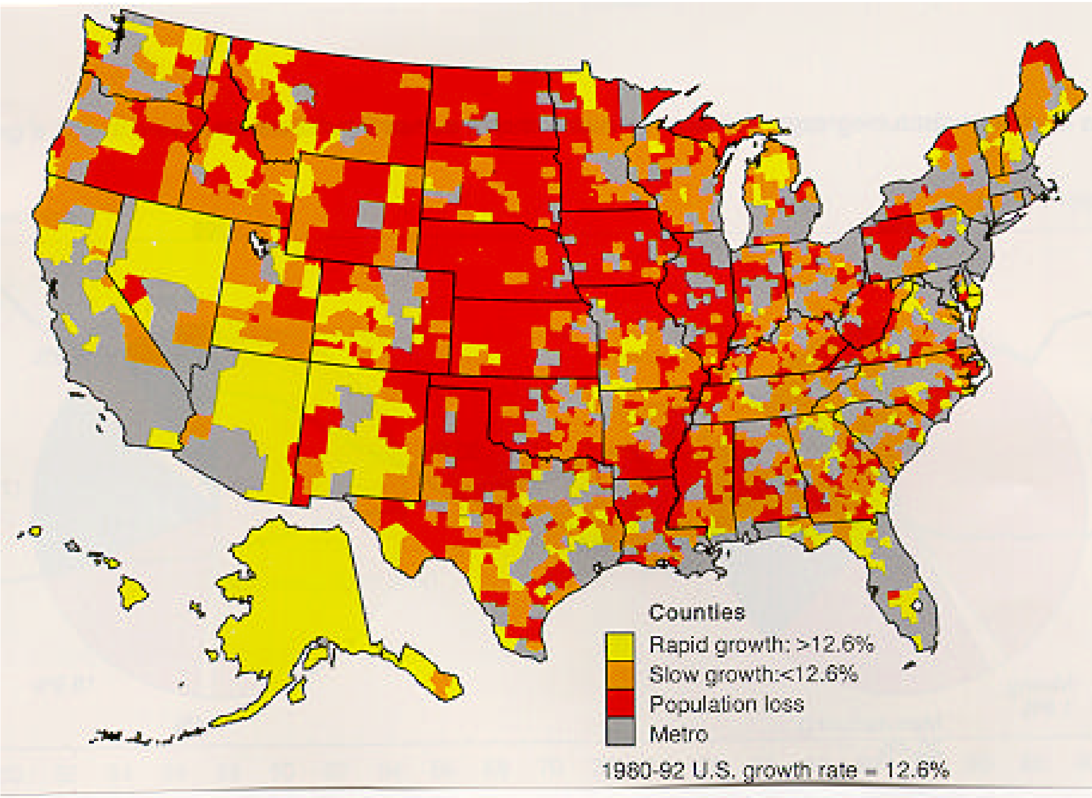
Rural Population

Growing in some areas, but declining in others.

The United States, like the rest of the world, is steadily becoming more urban. Two national censuses illustrate the point dramatically. For the first 140 years of the Nation's existence, most Americans lived in open country and small towns. The 1920 Census was the first to record that urban people outnumbered those living in open country and small towns. Just 70 years later, the 1990 Census recorded not only that most Americans lived in urban areas, but that they lived in metropolitan areas of over 1 million people. The Nation today is not only urban, it lives predominantly within major metro areas.

After a long period of little or no growth as the farming and mining populations decreased, rural and small-town areas grew faster in the 197Os than urban and suburban America. That turn-around showed the continuing potential for rural America to thrive economically and retain its people. Industries moving to rural areas, growth of recreation and retirement areas, renewed mining activity, urban workers living in and

Population growth varied widely across rural America.

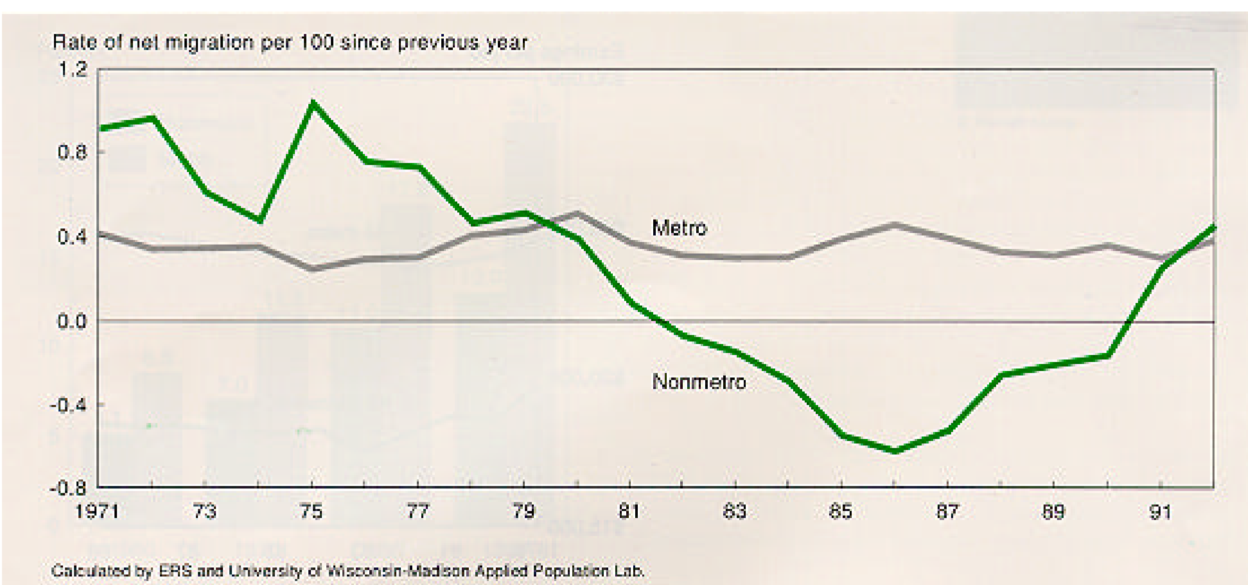


commuting from rural areas, and dissatisfaction with urban conditions all contributed to the resurgence.

In the 1980s, this trend reversed under the weight of the lengthy general business recession, foreign industrial competition, the farm crisis, and fewer retirees moving to rural areas. The loss of well-educated young adults (a continuation of a long-term trend) was indicative of the poorer prospects that people saw for rural communities.

The 1990s, thus far, have seen an encouraging rebound for rural areas. Softness in the national economy has been more urban than rural in character. Nonmetro unemployment rates are below those in metro areas. Although a majority of farm-dependent counties are still losing people, the losses are much lower than in the past. Areas with recreation and retirement development have grown substantially. Rural areas near growing urban areas have also grown. But while there are some encouraging signs overall, there is still a wide range of conditions and trends across rural areas, with each area facing its own problems and opportunities. ■

After attracting new residents in the 1970s, nonmetro areas reverted to their long-term trend of outmigration in the 1980s. So far in the 1990s, rural areas have seen population gains through inmigration.



Rural Well-Being

Some improvement, but gaps remain.

Many of the changes in rural America have been positive. Compared with the past, many of the conditions in rural areas have improved. Electricity, telephone service, and the highway system-and the development they promoted -- are a few of the most visible improvements.

Rural families are also better housed today and more likely to own their own homes than in the past. Only 2 percent of full-time occupied housing in rural America was substandard (lacking complete plumbing facilities) in 1990. Fifty years ago, nearly 75 percent of rural homes failed this measure of adequacy. Crowding is also less of a problem for rural households. Today, only 2 percent of households live in a home with fewer rooms than the number of household members, down from 25 percent of households in 1940. The rate of home ownership among rural households has also improved, increasing from one-half in 1940 to three-fourths today.

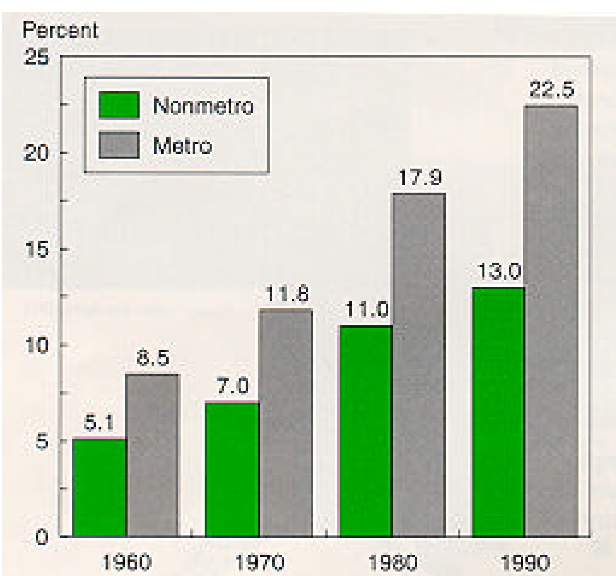
In a number of ways, rural areas have also gained ground on urban areas. High school completion rates, for example, have improved in rural areas and are now close to those found in urban areas.

The earnings gap between metro/nonmetro jobs persists and widens...

Gaps remain, however. Real earnings per job, an indicator of the strength of the economy and its ability to provide good jobs for its educated youth, remain consistently and substantially lower in rural areas than in urban and declined by 6.5 percent from 1979 to 1989. Similarly, college completion rates reveal a rural challenge. Compared with urban areas, far fewer rural residents are completing the education that is increasingly necessary for success in today's economy. And increases in population subgroups prone to economic disadvantage -- families headed by single mothers and minorities -- mean that more people are at risk of falling behind.

Underlying this overall picture are wide variations throughout rural America. The rural experience is very different from one part of the country to another. Some rural areas simply have not enjoyed many of the benefits of progress over the last 50 years. They have largely been left behind, still struggling with poverty, unemployment, inadequate infrastructure, and a lack of viable economic opportunities. Others, that have seen improvements, lack the resources and skills necessary to compete in the future economic environment. These, if they remain unprepared, will likely be left behind.

...as does the gap in college completion rates.



To understand the complexity of the challenge to rural America, one must understand the diversity of rural America. ■

Rural Diversity

Different challenges, different solutions.

Rural America is diverse in many ways. As we have seen, no one industry dominates the rural economy, no single pattern of population decline or growth exists for all rural areas, and no statement about improvements and gaps in well-being holds true for all rural people.

Many of these differences are regional in nature. That is, rural within a particular geographic region of the country often tend to be similar to each other and different from areas in another region. Some industries, for example, are associated with different regions -- logging and sawmills in the Pacific Northwest and New England, manufacturing in the Southeast and Midwest, and farming in the Great Plains. Persistent poverty also has a regional pattern, concentrated primarily in the Southeast. Other differences follow no regional pattern. Areas that rely heavily on the services industry are located throughout rural America, as are rural areas that have little access to advanced telecommunications services. Many of these differences -- regional and nonregional -- are the result of a combination of factors including the availability of natural resources; distance from and access to major metropolitan areas and the information and services found there; transportation and shipping facilities; political hstory and structure; and the racial, ethnic, and cultural makeup of the population.

The result: Rural areas differ in terms of their needs and the resources they possess to address those needs.

To explain some of these differences, the rest of this report examines six types of nonmetro counties. These types were chosen because of their importance to the rural economy and/or rural development policy. Three of the county types -- farming counties, manufacturing counties, and services counties -- are based on economic specialization and are mutually exclusive. That is, the types are defined by a county's economic dependence on a particular industry. The other three types -- retirement-destination counties, Federal lands counties, and persistent poverty counties -- are based on their special relevance to policy and are not mutually exclusive. Population shifts and the use of natural resources, ownership of land and its effects on rural people and communities, and the issues associated with low-income people are all themes that merit special attention.

For each county type, information is provided on income and employment and other relevant socio-economic indicators. Each section also contains discussion on what it means to people to live in a county of that type, with a special focus on what the future might hold. ■

Once, the vast majority of rural counties depended on farming as their primary source of income. Today, fewer than a quarter do, and these farming-dependent counties are home to only 9 percent of the rural population.

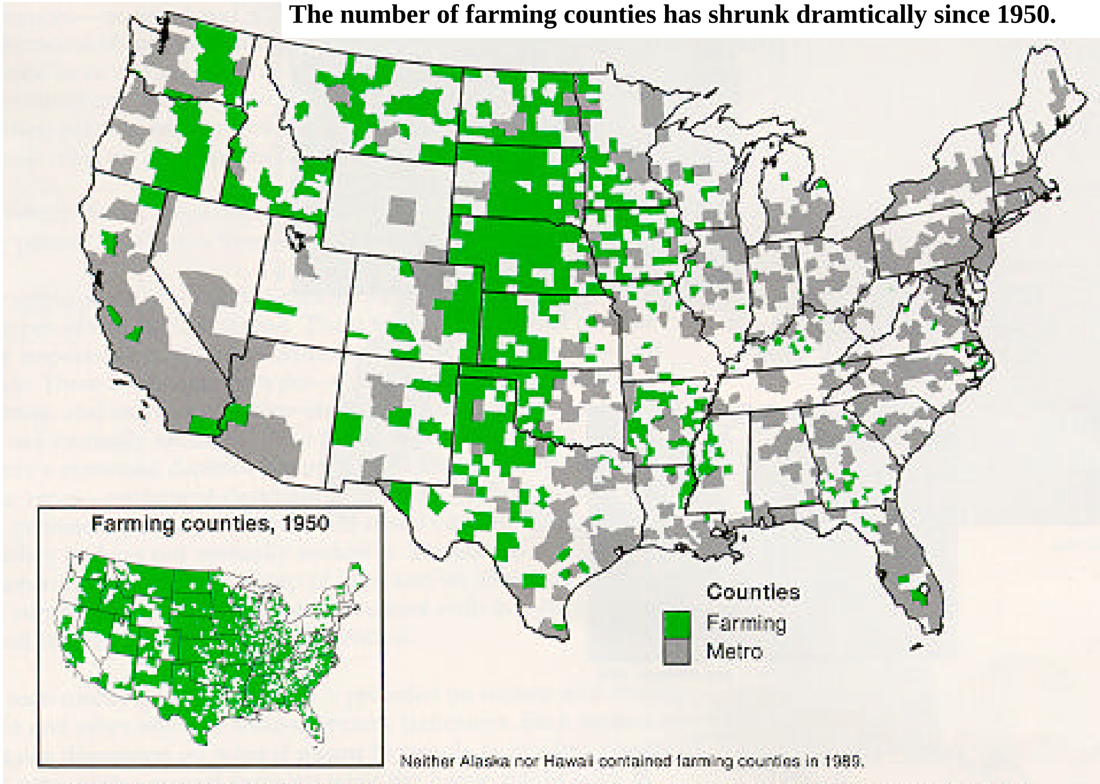
Concentrated in the Great Plains, these 556 counties derive 20 percent or more of their earned income from farming; for one county the figure was 89 percent. Even in these counties, however, nonfarm sectors are a major source of employment and income, providing nearly 80 percent of the jobs in farming-dependent counties. Those jobs are held by farmers and nonfarmers alike. Many farmers and farm families depend on nonfarm jobs and incomes to make ends meet.

The decline in the number of farming-dependent counties is, in part, a consequence of agricultural success. Increases in farm productivity -- through advances in production technology, crop science, and management -- have led to decreases in farm employment Simply put: fewer people are needed to produce an increasing amount of farm goods.

In addition to changes in farming, the remoteness of these counties (the most rural of the county types discussed here) creates a barrier to development. With very few urban centers or nearby major metropolitan areas, these counties have limited access to the information, innovation, trade, services, and finance that drive today's economy.

In addition to the distances between communities, low average population densities (11.8 persons per square mile compared with 36.3 for all nonmetro counties) also increase per capita costs of infrastructure and other investments, making it hard for people in these communities to maintain transportation systems, utilities, public institutions, and other services that urban areas take for granted.

The number of farming counties has shrunk dramtically since 1950.



As farming employment has declined, other types of industry have not replaced all the jobs that were lost. Thus, many young people have left to seek jobs elsewhere, often moving to a different part of the country.

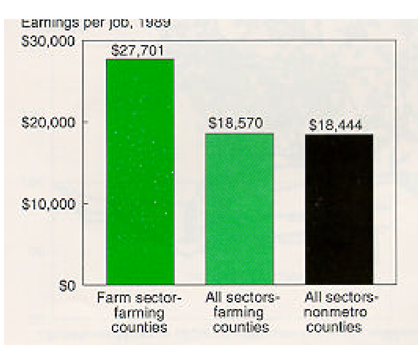
Despite the decline in jobs, income levels in farming-dependent counties compare favorably with other nonmetro counties. Average per capita income in these counties was higher in 1989 than the average of all nonmetro counties, though considerably lower than the metro average. Within the farming sector, earnings per job in these counties were $27,701 in 1989, substantially above the nonmetro counties as a group. However, these figures can mask the fact that even within the relatively well-off farming counties, some people may have much lower incomes.

Farming counties lagged behind other nonmetro counties in creating jobs. Total employment declined 1.2 percent and, consistent with national trends, farm jobs declined by 111,000 (19.4 percent) from 1979 to 1989. In these counties, new jobs are not being created fast enough to replace those lost in farming.

Population (as well as population density) in these counties is relatively low, averaging only 8,400 in 1990, compared with 22,000 for all nonmetro counties. Outmigration continues to take its toll on these already small and low-density populations. From 1980 to 1990, 80 percent of farming-dependent counties lost population. During the 1980s, the average rate of outmigration was 11 percent-highest among all nonmetro county types and more than double the nonmetro average of 4.4 percent. The loss of younger, well-educated people is particularly significant, as they leave to seek jobs that are not being created locally. The 18- to 34-year-old population in farming counties declined 17 percent on average from 1980 to 1990. This decline exacerbated the already high ratios of nonworking-age to working-age people. For every 100 working age adults, 87 residents were in the dependent population: those 17 years old or younger plus those 65 or older.

Stabilizing population, enhancing job opportunities, and providing public services in these counties is a major rural development concern today. The well-being of residents and communities hangs in the balance. If historical and current trends continue, however, the future of farming-dependent counties will be one of further declines in population -- especially among the working-age and well-educated -- and farm employment. As population declines, the per unit costs of infrastructure and such services as health care and education will increase. As farm employment declines, other types of employment will need to be found to replace those jobs. However, the outmigration of working-age and well-educated people may act as a barrier to creating and maintaining those other economic activities. ■

In farming counties, farm jobs pay well...



...but there are fewer and fewer of them.

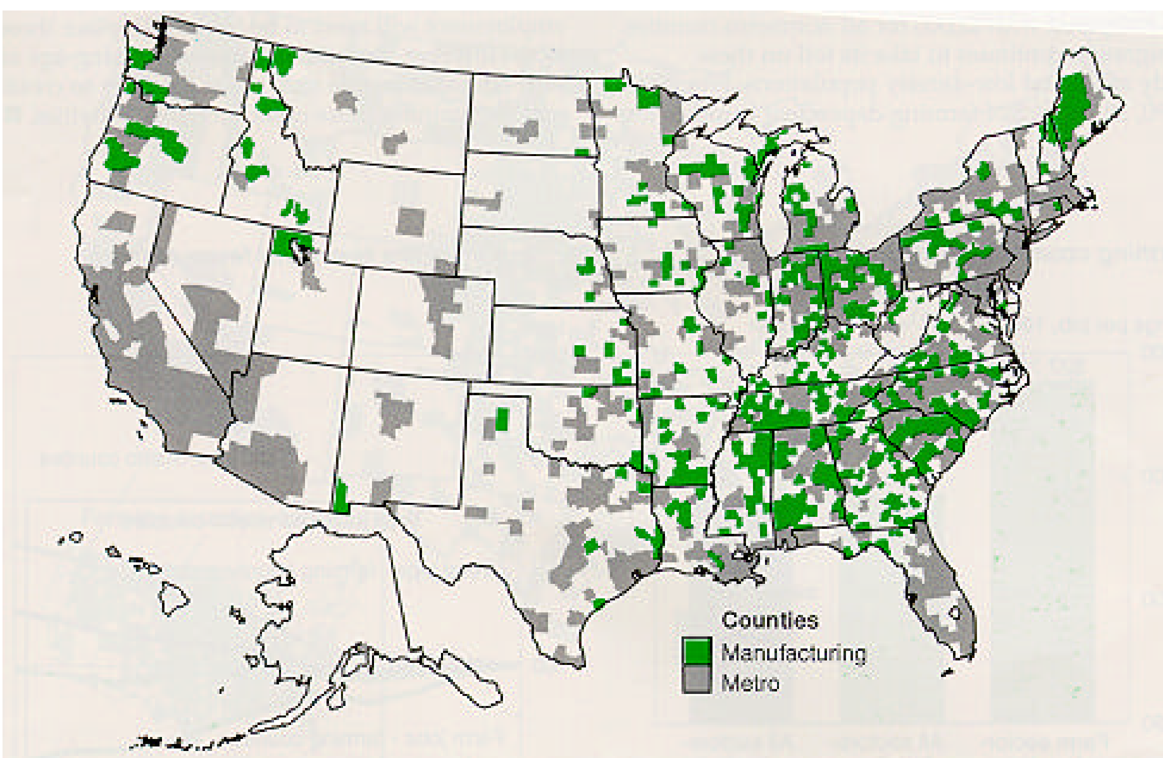
Nationwide, manufacturing employs more than twice as many rural people as does farming. Contrary to popular opinion, rural manufacturing is not primarily involved in the processing of food or the provision of farm inputs. In 1991, only about 13 percent of rural manufacturing was closely tied to farming[2]. In fact, in many rural counties, manufacturing has been replacing farming as the primary economic activity for several decades.

Of the county types based on economic specialization, manufacturing-dependent counties are second in number only to farming counties. These 506 counties are home to 31 percent of the rural population. Concentrated in the eastern half of the Nation -- particularly the Southeast -- these counties receive 30 percent or more of their earnings from manufacturing.

As with farming, forces of change are at work in manufacturing. On the one hand, routinizafion of production methods; readily available technology; world-wide improvements in transportation, education, and health; and relaxation of trade rules combine to enable many companies to locate their production facilities anywhere in the world. Today, everything from auto parts to computer chips to clothing is made abroad and shipped to the United States. Such conditions increase the global competition for low-skill, low-wage manufacturing jobs -- the type of manufacturing jobs most prevalent in rural areas -- and have the potential for pushing real wage rates down in rural areas facing that competition.

On the other hand, the highest returns (and therefore, higher paying jobs) in manufacturing in this era of increasing global competition go to makers of high-value products with short production runs, quick turnaround, and products in so-called niche markets -- for example, specialty medical equipment and supplies,

Manufacturing counties are home to nearly one-third of the rural population.



electronic instruments, and even custom-made furniture. The ability to compete in these markets, however, requires access to information, finance, and transportation. And, since these assets tend to be more readily available in urban areas than in rural, urban firms often have the upper hand.

Thus, rural manufacturers and their employees are caught between two types of competition: low-wage, low-skill manufacturers abroad and high-wage, high-skill manufacturers in metropolitan areas.

The economies of the manufacturing counties improved slightly during the 1980s, due mainly to gains made in the latter part of the decade. However, these gains were primarily in the fast-growing services and government sectors, rather than in the manufacturing sector. In the services sector of these counties, total earnings increased 15 percent and jobs grew 46 percent between 1979 and 1989. In contrast, throughout most of the decade, manufacturing jobs showed a slow decline, with growth beginning after 1987. As a result, manufacturing jobs in these counties grew 2.8 percent for the decade.

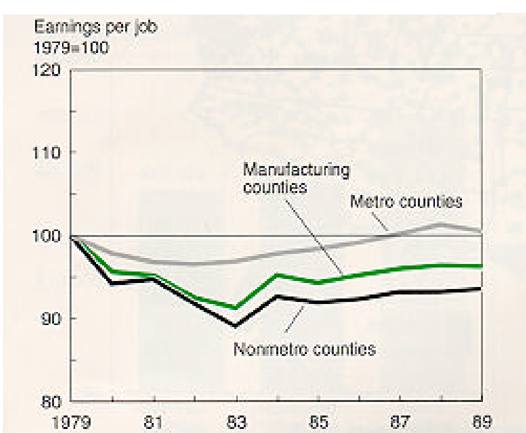
Following a general trend for nonmetro areas as a whole, manufacturing counties experienced a decline in earnings per job over the decade. Even with this decline, however, earnings per job in these counties have been consistently higher than in nonmetro counties as a whole.

The population of manufacturing counties grew by 1.5 percent from 1980 to 1990. Manufacturing counties in the Midwest, however, lost population.

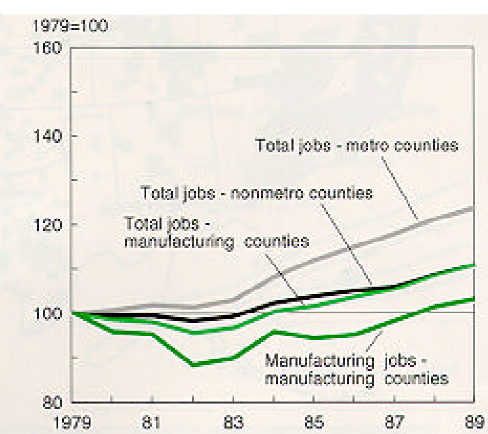
Manufacturing counties are more likely than other nonmetro counties to have larger urbanized populations, to be adjacent to urban centers, and to have high population densities. Thus, they tend to have greater access to services that are important to the success of rural business. That fact notwithstanding, the largest growth rate of manufacturing jobs occurred in the most rural manufacturing counties.

Competition from both foreign and metropolitan manufacturers will likely continue to be a significant factor in the future of rural manufacturing counties. Unless new ways are found to improve the competitiveness of rural manufacturing -- through production modernization, improved management practices, creation of networks for cooperation, and improvements in worker skills -- real earnings per job may continue to suffer and, consequently, the well-being of residents to lag. ■

Jobs in manufacturing counties tended to pay more than in nonmetro counties as a whole throughout the decade.



Job growth in manufacturing counties came chiefly from the nonmanufacturing sectors.



Growth in the services sector has been the dominant force in nonmetro (as well as national) industrial trends over the past two decades, giving rise to the popular term "service economy." The services sector includes transportation and public utilities, wholesale and retail trade, finance, insurance, real estate, agricultural services, and other services. From 1979 to 1989, over 3 million nonmetro services jobs were created, accounting for 83 percent of new nonmetro jobs.

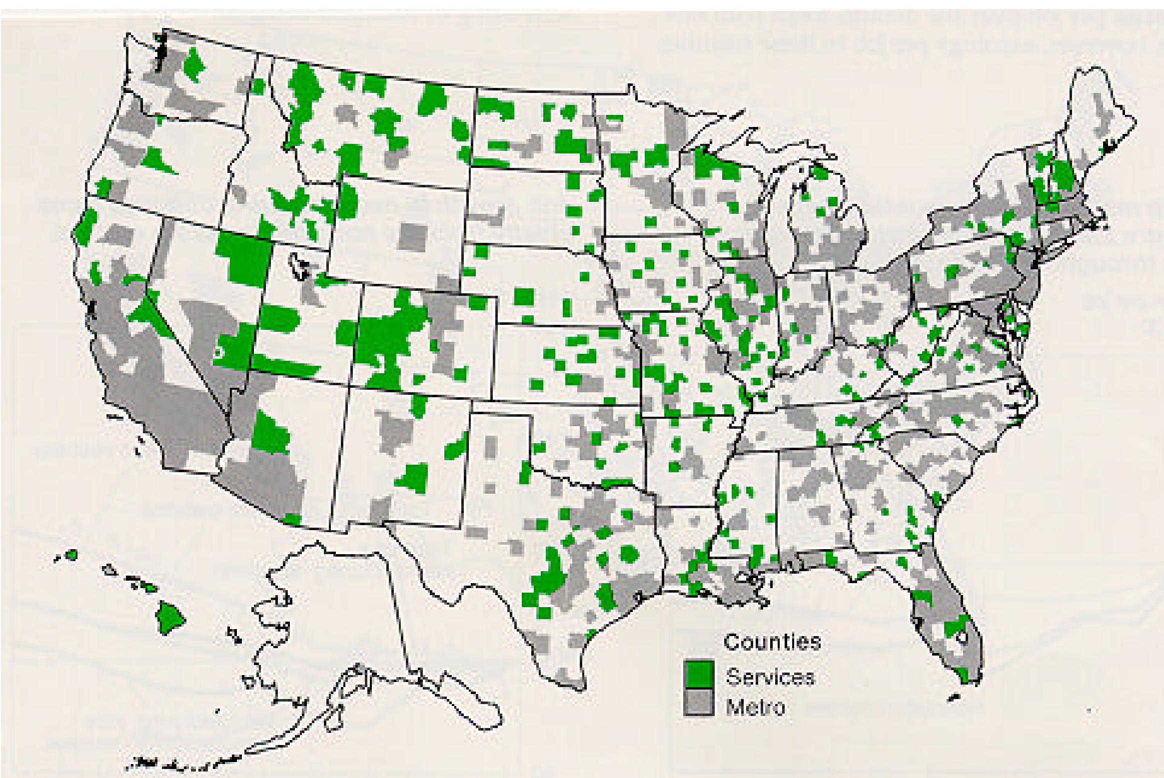
The 323 services-dependent counties, as defined here, derived 50 percent or more of their earned income from services jobs over the 3-year period 1987-89. Unlike farming and manufacturing counties, there is no regional pattern to the location of services counties. Rather, they are scattered across the Nation fairly evenly.

Depending on their location, degree of urbanization, and access to a metro area, services counties are likely to play different roles in an area's economy. Services counties in the Great Plains are more likely to act as regional trade centers to surrounding rural areas that lack large urban centers. Services counties near natural amenities are more likely to act as providers of services geared toward the needs of recreation, tourism, and retirement.

Seventy services counties (22 percent) were also retirement counties and 60 (19 percent) were also Federal lands counties. This is not surprising given the dominant role that services play in the economies of those county types.

The economies of services counties did well during the 1980s. Total real earnings grew by nearly 9 percent (more than twice the rate for nonmetro counties as a whole), and earnings from services grew by 24 percent (nearly twice as fast as the nonmetro average). The number of jobs in services counties grew slightly faster (both in

Services counties did well and grew rapidly during the 1980s.



total jobs and services jobs) than in nonmetro counties as a whole. Gains in two sectors – 800,000 new services jobs and 76,000 new government jobs -- dominated job growth in the services counties. However, the economic performance of services counties presents something of a dilemma.

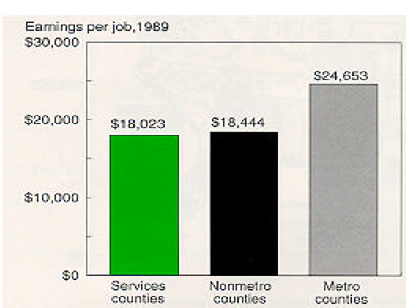
On one hand, services counties had, on average, lower unemployment, a greater share of residents with high school educations, higher median family income, higher per capita income, and higher per capita earnings than the nonmetro average.

On the other hand, earnings per job were slightly lower and declined faster than in nonmetro counties as a group (8 percent as compared with 6.5 percent) during the 1980s. In fact, for nonmetro areas as a whole, earnings per job in the services sector were the lowest of all industrial sectors examined. Services jobs in services counties, however, tended to pay better than services jobs in other counties. This may be partially explained by the role of services counties as regional trade centers and support centers for recreation and retirement areas and the higher paying services jobs -- health care professionals, attorneys, engineers, recreational outfitters, etc. -- that accompany those roles. The dilemma of high incomes and low earnings per job may be partly explained by a higher than average ratio of "property income" (dividends, interest, and rent) to earned income that raises income levels despite low earnings per job. This explanation is consistent with the fact that 70 services counties are also retirement-destination counties and retirees often have higher levels of property income than younger people. Workers holding more than one low-paying job may also be responsible. For example, a services worker might hold one full-time and one part-time job, neither paying very high wages. Finally, people with higher incomes may commute to higher paying jobs in other -- possibly metrocounties.[3]

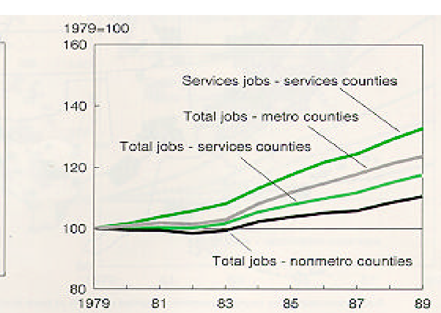
Population in services counties, on average, grew significantly (6.3 percent versus 0.6 percent nonmetro average) during the 1980s. Part of that population growth was due to inmigration, a rarity for rural counties. The growth in population is not surprising given the good economic performance of these counties, since the two usually go hand in hand.

Nationally and internationally, growth in the services industries will likely continue in the future. The ability of rural areas to benefit from that growth will depend on their individual situations. Rural areas near natural amenities will probably see increasing demand for services associated with recreational activities and retirement populations. Rural areas that act as regional centers in sparsely populated parts of the country will depend on the existence of a population base large enough to demand those services. Therefore, these centers may be in trouble, if population loss trends in their surrounding areas continue. ■

Jobs in services counties tended to pay slightly less than in nonmetro counties as a whole...



...but job growth in services counties was strong.



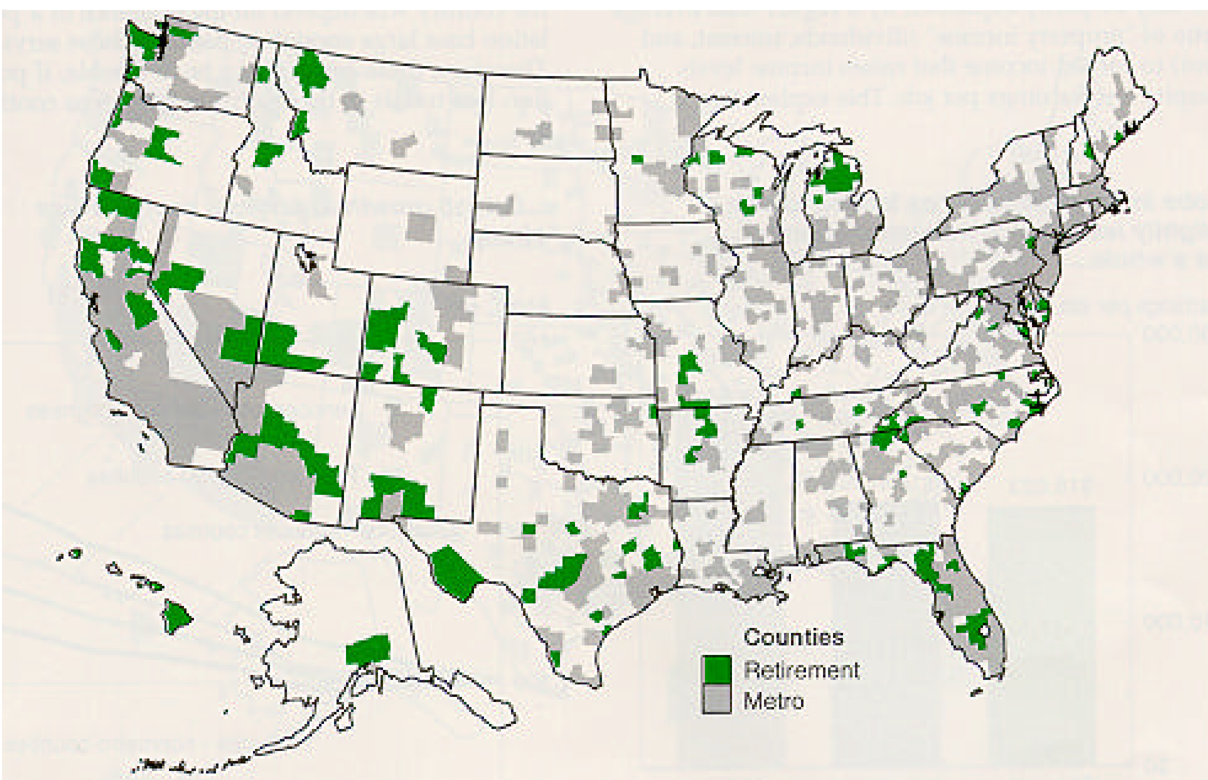
The presence (or absence) of natural amenities is becoming increasingly important to the economic well-being of rural areas. With such amenities as a mild climate, mountains, coastlines, and lakes, a rural area can attract retirees, tourists, and recreationists, as well as some firms and self-employed professionals who place a high value on the quality of living offered by these amenities. In turn, the economic activities -- particularly services -- that these people and firms generate are becoming increasingly important sources of employment and income.

Examined here are "retirement-destination counties," counties -- mainly in the South and West -- that experienced 15 percent or more inmigration of people age 60 and older in the 1980s. These counties are generally more rural than other nonmetro counties. In addition to being located near amenities, these counties also tend to be near military bases, reflecting the desire of military retirees to be near medical and shopping facilities located on the bases.

Along with natural amenities, several other factors have contributed to the increased migration to these areas: improved health of older people, earlier retirement ages, higher retirement incomes, some preference for smaller communities, and improvements in transportation and communications.

While generally viewed as a positive development for rural areas, the influx of retirees and other inmigrants is not problem free. Increased demand for infrastructure (roads, water and sewer service, etc.) and social services, change in local cultural values, and escalation of property values and housing costs are among some of the factors associated with the trend that can be troublesome to long-time residents.

Natural amenities, such as a mild climate, mountains, and seashores, draw tourists and recreationists, as well as retirees, to retirement-destination counties.



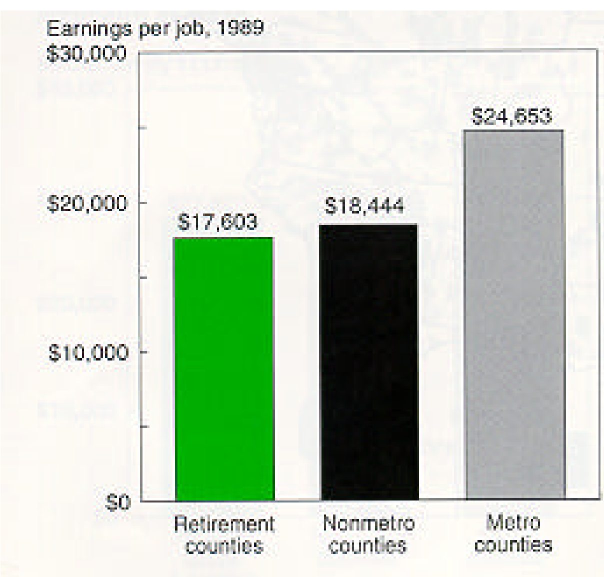
Economically, these counties did very well during the 1980s. As a group, they had the highest rate of earnings growth (26 percent) and job growth (34 percent) of any nonmetro county type. In fact, nearly all the retirement counties had job growth.

The job growth rate is explained, in part, by rapid growth in services, government, and construction jobs in these counties. Nearly three-fifths of the jobs in the retirement counties are in the services sector. Due in part, however, to the dominance of services sector jobs (even though some of them may be in higher paying services), earnings per job are slightly lower in retirement counties than in nonmetro counties as a group.

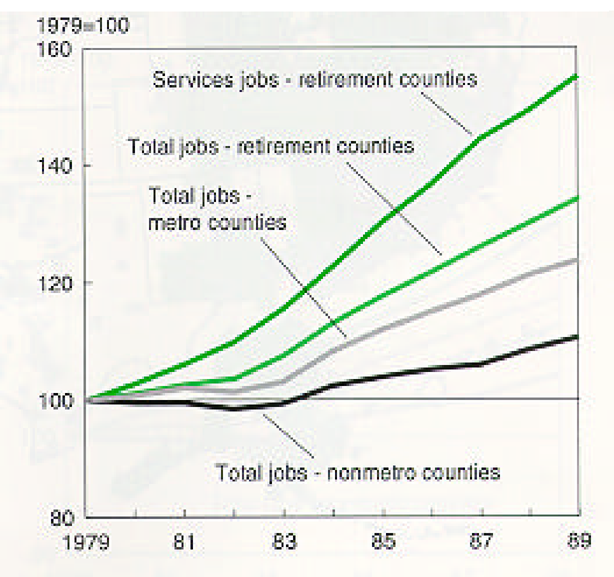
Population grew an average of 23 percent in these counties in the 1980s, far exceeding the 0.6 percent nonmetro average. The number of people age 65 and over grew by 45 percent. The size of the younger population grew as well, in part because of job growth in recreation and tourism and in services catering to the needs of retirees.

Management of a growing population and the pressure it puts on infrastructure and public services, property values, housing costs, and community composition and values, as well as the pressure put on the natural amenities that serve as the drawing card, will be a major challenge for retirement counties. The prevalence of low-skill, low-wage jobs may not adequately provide for the needs of workers, especially if an influx of wealthier retirees drives up demand (and prices) for housing and other essentials. ■

Earnings per job in retirement counties were about 5 percent less than in nonmetro counties as a group.



However, job growth in retirement counties exceeded even the metro rate; growth in services jobs in retirement countis was even greater.



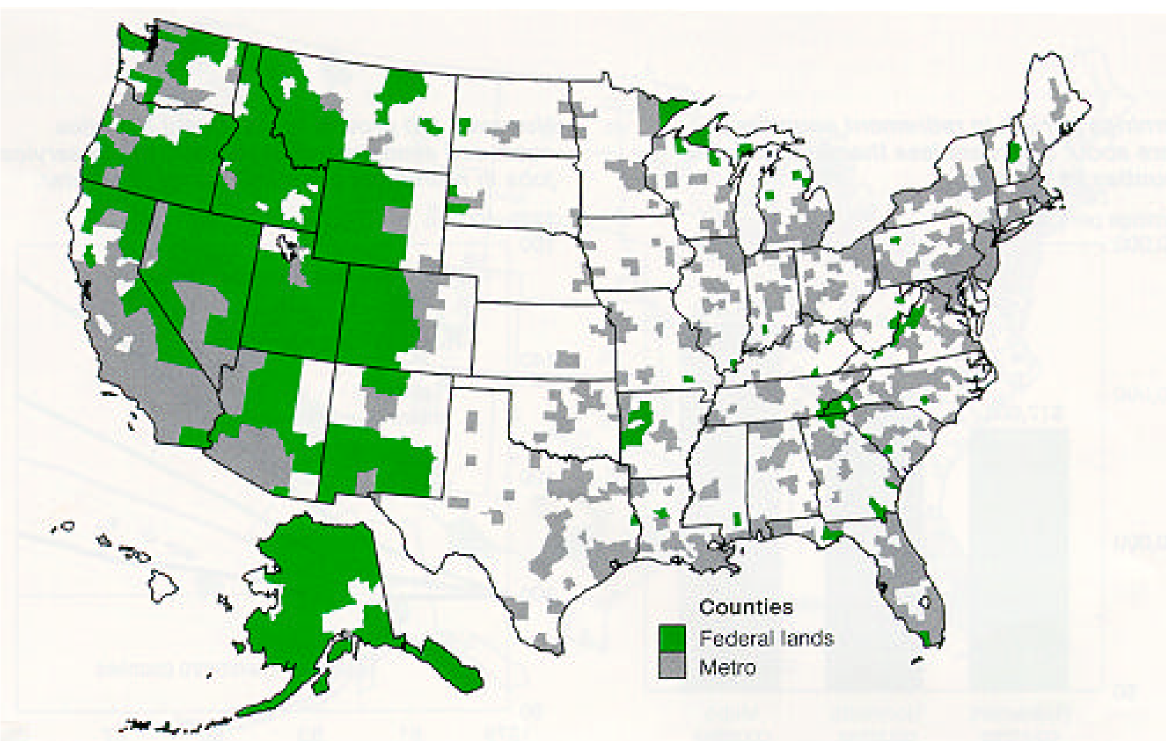
Land use, property rights, and protection and use of natural resources are issues of great importance to the Federal lands counties -- counties in which 30 percent or more of the land is owned by the Federal Government. In 1987, there were 270 such counties, located primarily in the West. The amount of federally owned acreage in these counties ranged from 30 to 99 percent.

Because the Federal Government owns much of the land, these counties are significantly affected by Federal policies and regulations dealing with land, the environment, tourism, and recreational activities. The debate on such policies and regulations is often couched in terms of economic development versus environmental protection. In reality, the debate is primarily about who has the right to use and benefit from Federal lands, how those lands can be used, and who pays for those benefits. A wide range of people and activities compete for that right. Ranchers, miners, loggers, recreational users, and those concerned with the preservation of wilderness all have a stake in the governance of Federal lands. And as the West grows, its population changes, and the demand on its natural resources increases, the level of debate will likely rise, often pitting recent urban emigres against long-time local residents.

Economically, Federal lands counties fared slightly better as a group than other nonmetro counties in the 1980s. Median family income was higher than the nonmetro figure, although still well below metro levels, and the average poverty rate (15.8 percent) was the lowest of all county types.

Job growth in these counties was also strong. The average growth rate in services jobs in Federal lands counties outpaced even the average total job growth rate in metro areas, and the overall job growth rate in these counties was

Concentrated in the West, Federal lands counties are affected by policies on land and resource use.



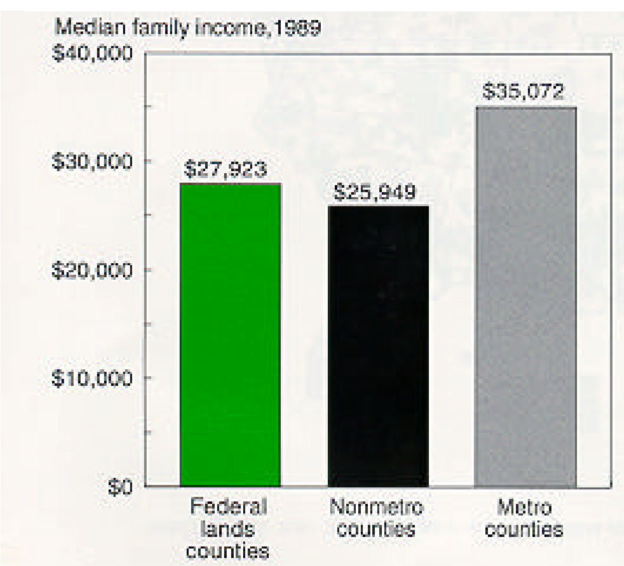
faster than the nonmetro rate. However, earnings per job declined over the decade by nearly 11 percent, significantly more than the 6.5 percent decline for nonmetro counties as a group. Nearly 70 percent of jobs in the average Federal lands county were in the services or government sectors (hence the fact that 60 Federal lands counties were also services counties). Of the 554,000 new jobs created in these counties, 429,000 (77 percent) were in the services sector.

The success of the services sector in these counties is, in part, associated with the growth in tourism and recreation that these areas have experienced. As the American public becomes increasingly mobile and recreation-minded, the demand for services in these counties increases. The accompanying jobs range from seasonal jobs serving tourists to full-time government land managers. Thus the pay scale varies widely also.

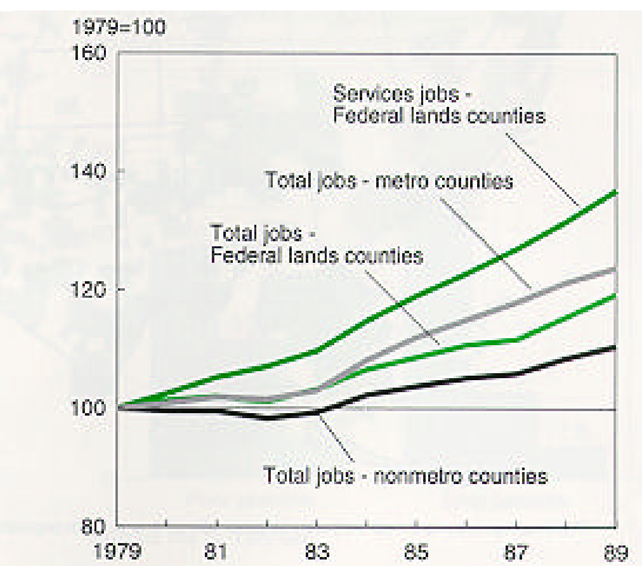
Population also grew in these counties, significantly outpacing the nonmetro average (9 percent versus 0.6 percent). This population growth was due in part to tourism and retiree attraction (58 Federal lands counties -- 22 percent -- are also retirement-destination counties). Reflecting the overlap with the retirement counties, the number of people age 65 and over grew by 33 percent. The number of working age people also grew.
Population density in these counties is low, averaging only 15.4 persons per square mile. This fact is not surprising given the relative lack of development and small populations in the large western counties. Only farming counties, with 11.8 persons, had lower average density. This does not mean, however, that population is spread evenly and thinly across the counties. About 14 percent of the counties had towns and cities of 20,000 to 50,000 people.

The issues facing Federal lands counties are inseparably intertwined with Federal policies and regulations regarding the use of those lands. The degree to which particular groups of people benefit from growth in these counties depends, in part, on their relationship to the natural resource base and how those relationships are affected by policies and regulations. However, as the income and job situation suggests, these counties are, in the aggregate, doing well, even while some in the counties are not. ■

Family income in Federal lands counties was nearly 8 percent higher than the nonmetro average.



Total job growth nearly matched the metro rate.



The number of counties with high concentrations of poverty has decreased dramatically over the last 30 years. In 1960, a total of 2,083 rural counties had 20 percent or more of their population living below the poverty level. By 1990, the number had shrunk to 765, a decline of nearly two-thirds and an indication of the remarkable reduction of poverty across rural America. [4]

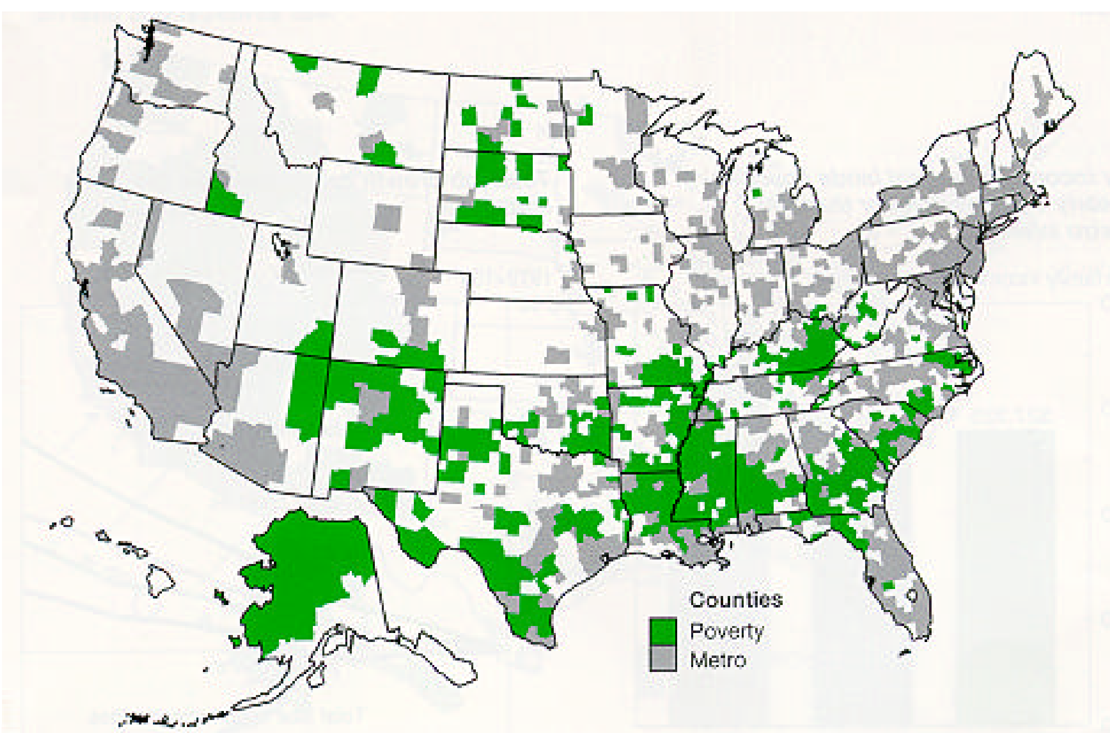
For 535 of those counties, however, poverty continues to be a long-term problem. The persistent poverty counties discussed here are those in which 20 percent or more of the population were below the poverty level in each of the years 1960, 1970, 1980, and 1990. Actual 1990 poverty rates in these counties ranged from 20 to 63 percent with an average of 29 percent, compared with the nonmetro average rate of 18.3 percent. For many of these counties, there has been some reduction in poverty, although their poverty rate is still high enough to keep them in the persistently poor category.

These counties are heavily concentrated in the Southeast, Appalachia, and the Southwest, with others scattered on Native-American reservations in the North and West. The persistent poverty counties (24 percent of all nonmetro counties) contain 19 percent of the nonmetro population and 32 percent (2.7 million) of the nonmetro poor.

As would be expected, income levels in poverty counties were considerably lower than in other counties. Per capita income in 1989 lagged the nonmetro average by $2,500. Median family income lagged by more than $5,000, placing it, along with earnings per capita, at or near the bottom of all county types.

Unemployment rates in these counties were the highest of the six types examined in this report. The average unemployment rate in 1990 was 8.5 percent, considerably above the 6.6-percent nonmetro average. It is important to note, however, that poverty is not simply a problem of

Persistent poverty counties are concentrated in the Southeast, Southwest, and Appalachia.



unemployment. Unemployment is only part of the problem. The prevalence of low-skill, low-paying jobs in rural areas means that the wages of many rural workers are not high enough to pull them out of poverty. In fact, the Nation's working poor are more likely to live in rural areas then urban. Twenty-five percent of the Nation's poor live in rural areas; about 30 percent of the poor who are full-time, full-year workers live in rural areas.

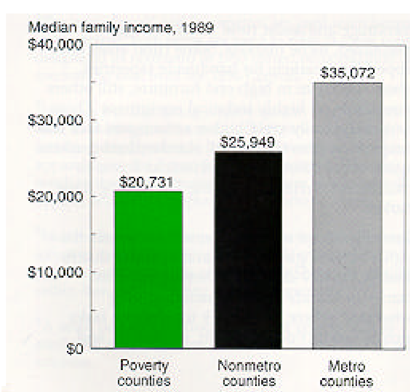
While the number of jobs grew by 6 percent in these counties during the 1980s, that rate was just over half the rate for nonmetro counties as a whole (10.6 percent).

Poverty counties tend to have somewhat smaller and less urbanized populations than do other county types. Over half of the counties were not adjacent to a metro area, suggesting limited access for residents to jobs in urban centers, especially since public transportation service is generally lacking and low incomes limit the possibility of private transportation.

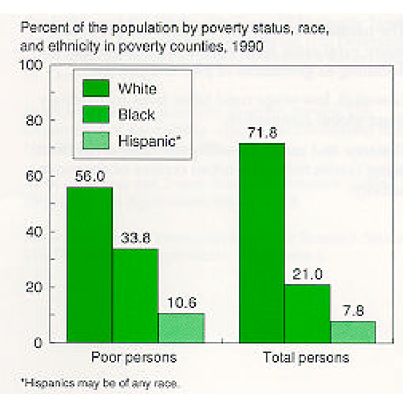
Poverty counties have disproportionate numbers of people with characteristics that make them prone to economic disadvantage. On average, these counties have large numbers of people without a high school education -- putting them at risk of being unprepared to participate in the economy -- and people living in female-headed households. These counties also have higher than nonmetro average proportions of Blacks and Hispanic -- groups that historically have had trouble gaining access to economic opportunities. Poverty is not, however, strictly a racial issue. As noted above, education and family status are important factors. Furthermore, nearly 80 percent of the nonmetro poor are, in fact, White. In poverty counties, that figure is 56 percent. Given their share of the population, however, Blacks and Hispanics do make up a disproportionate share of the poor in poverty counties and in nonmetro counties as a whole.

By definition, the major concern in these counties is that high proportions of their residents live on incomes below the Federal poverty level. Hand in hand with that poverty is often a lack of basic necessities such as health care, good nutrition, education, and essential public services. These needs are different from, but related to economic development needs. Improvements in these basic necessities are essential if people in these counties are to be healthy, educated, productive workers. Likewise, higher incomes from better paying jobs can enable people to obtain these basic services. Resolution of long-term poverty, therefore, requires that both types of needs be addressed. ■

Family income in poverty counties is only 80 percent of the nonmetro average, 60 percent of the metro average.



The majority of the rural poor are White, but Blacks and Hispanics make up a disproportionate share of the rural poor.



Understanding rural America is no easy task. It is tempting to generalize and oversimplify, to characterize rural areas as they once were or as they are now in only some places. As this report has shown, however, understanding rural America requires understanding the ongoing changes and diversity that shape it. Likewise, policies, if they are to be effective in assisting rural areas, will have to recognize the realities growing out of that change and diversity.

The diversity of rural America means different areas have different needs.

The economies of individual rural areas differ, as do the resources upon which they are built and the opportunities and challenges they face. Some have participated in the economic progress of the Nation over the last half century, while others have not. Even among those that have benefited in the past, many are not well positioned to compete in today's global economy. Each of those types of areas has different needs. No single policy can sufficiently address the needs of all.

Still, there is an overall pattern of economic disadvantage in rural areas.

The historical and defining features of rural economies often constrain development. Regardless of other differences, efforts to assist rural areas must take into account these common rural characteristics:

- Rural settlement patterns tend to be small in scale and low in density.
- The natural resource-based industries on which many rural areas have traditionally depended are declining as generators of jobs and income.
- Low-skill, low-wage rural labor faces increasingly fierce global competition.
- Distance and remoteness impede rural areas from being connected to the urban centers of economic activity.

"High-amenity" rural areas, however, are growing.

Many rural areas with amenities such as mild climate, mountains, coastlines, and lakes are gaining population. These areas are attractive to retirees and tourists, and their influx has led to increases in employment -- especially in services -- and income for the areas. Areas with amenities, therefore, have a development asset, but as a result must deal with issues of managing their growth.

There is no single recipe for rural prosperity, but the potential is considerable and there are logical ways to promote development.

Because rural areas differ, no easy answers or "one size fits all" policies will work. In light of that, the following should not be viewed as a recipe or checklist of any kind. Rather, it is a set of principles that take into account the different rural conditions and trends discussed in this report and show promise in helping rural areas and people realize their goals. Because they are principles, the manner in which they are applied will vary according to the needs of individual situations.

- Improve the connections between rural and urban areas by improving infrastructure and the dissemination of information and the ability to use it. Advanced telecommunications, for example, while not a panacea, afford rural communities more economic opportunities by providing them with better access to information, markets, and services such as business and technical assistance, medical care, and educational opportunities.
- Encourage and assist rural firms to target specialized, niche markets. Some rural areas have tapped into markets for

handmade tapestries, others specialize in high-end furniture, still others concentrate on highly technical equipment. These markets typically yield higher returns and face less competition than traditional, standardized markets. Again, connections are important, as access to information is critical in finding and tapping these markets.

- Create "artificial scale economies" to counter the higher costs of government and business due to small-scale, low-density settlement patterns. Examples include "flexible manufacturing networks," where firms work together on tasks such as product development, marketing, and buying supplies; and "multi-community collaboration," where communities form a partnership to jointly buy services and equipment or provide municipal services. Both are ways to emulate economies of scale to reduce costs.

- Improve the competitiveness of rural firms by enhancing the core skills of both management and labor. Competitiveness in today's market increasingly depends on the ability to obtain and use information, technology, and new management techniques.

- The challenges facing rural America today are indeed diverse, complex, and changing. There is hope, however. Armed with accurate information and a clear understanding of the challenges, policymakers working together with rural citizens can meet those challenges. The vitality of rural America, its people, and its places can be maintained. With care and informed decisionmaking, rural America can continue to play a role of national importance -- contributing to the economic, social, cultural, environmental, and recreational well-being of all Americans. ■

Notes

[1]The terms "rural" and "nonmetro" are used interchangeably in this report. Both terms are used to refer to those counties designated as nonmetro in 1993 (based on population and commuting data from the 1990 Census).

[2]Includes manufacturing employment in food processing, food marketing, and farm input industries. Including manufacturing employment in leather and footwear, textiles, and apparel raises the figure to about 28 percent. However, much of the manufacturing employment in textiles and apparel is based on imported and synthetic fibers.

[3]Median family income, per capita income, and per capita earnings are reported for place of residence, rather than place of work, and thus reflect the well-being of residents rather than the well-being of local economies.

[4]A small part of the reduction in rural poverty can be attributed to poor nonmetro counties becoming poor metro counties.

For Additional Reading. . .

Cook, P.J. , and K. L. Mizer. *The Revised ERS County Typology: An Overview.* Economic Research Service, U. S. Department of Agriculture. Rural Development Research Report Number 89. December 1994.

Issues for the 1990's. Economic Research Service, U. S. Department of Agriculture. Agriculture Information Bulletin Number 664. September 1994.

Rural Conditions and Trends. Economic Research Service, U. S. Department of Agriculture. Vol. 4, No. 3.

Rural Development Perspectives. Economic Research Service, US. Department of Agriculture. Vol. 9, Issue 1.

Appendix table 1--Selected population, income, and employment characteristics for counties, by county type[1]

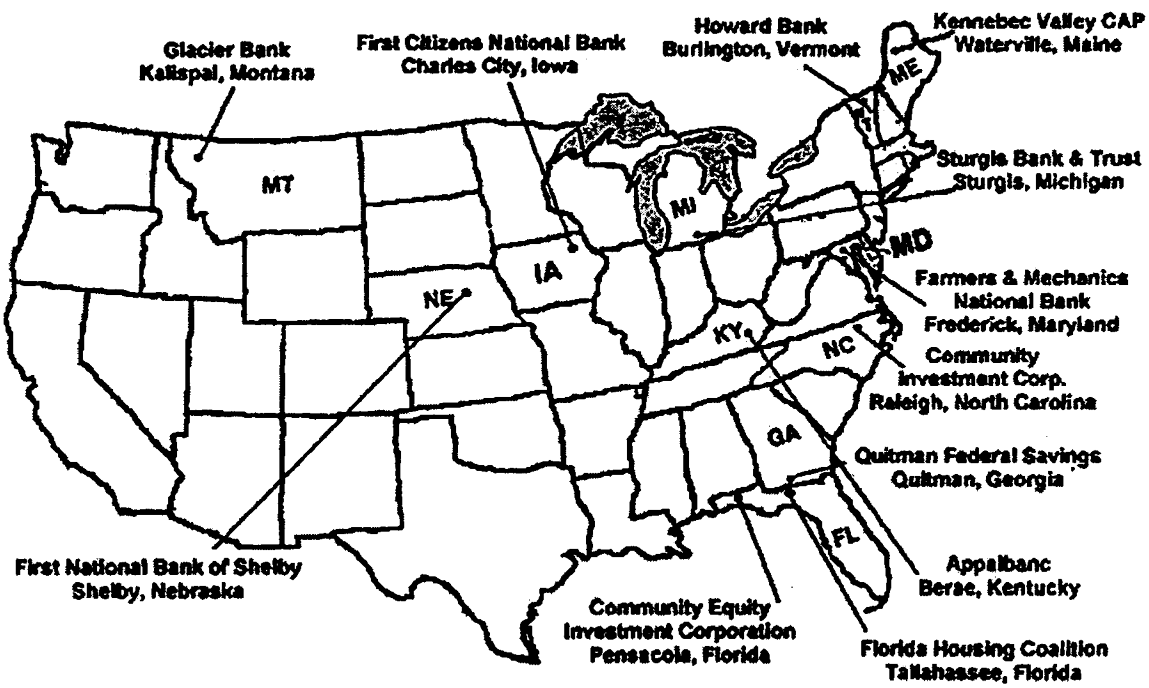
Item	Unit	Farming	Manufacturing	Services	Retirement	Federal lands	Poverty	Nonmetro	Metro
Counties	Number[2]	556	506	323	190	270	535	2,276	813
Nonmetro population, 1990	Percent[3]	9.1	31.0	18.8	10.2	10.7	18.8	100.0	--
Population growth, 1980-90	Percent[4]	-6.9	1.5	6.3	22.7	9.0	-1.2	.6	14.5
Persons in poverty, 1990	Percent[4]	18.9	16.9	16.5	16.3	15.8	29.1	18.3	12.2
Net migration rate, 1980-90	Percent[4]	-11.0	-3.1	1.3	18.3	.1	-7.0	-4.4	6.8
Persons per square mile, 1990	Number[4]	11.8	59.2	43.4	38.3	15.4	29.7	36.3	652.3
Per capita income, 1989	Dollars[4]	14,743	13,081	14,384	13,698	13,807	11,056	13,580	16,399
Per capita income growth, 1979-89	Percent[4]	11.6	13.2	10.6	12.6	8.3	11.6	10.4	15.1
Median family income, 1989	Dollars[4]	24,394	26,936	27,677	26,657	27,923	20,731	25,949	35,072
Median family income growth, 1979-89	Percent[4]	-1.6	.7	-.1	4.8	-1.0	-2.3	-1.3	4.7
Total earnings, 1989	Dollars[5]	39,170,938	145,575,789	87,491,170	41,654,450	50,310,088	65,709,312	441,726,020	2,746,177,980
Total earnings growth, 1979-89	Percent[3]	-6.1	6.0	8.5	25.9	6.8	.1	3.4	24.4
Total jobs, 1989	Number[6]	2,109,406	7,682,247	4,854,535	2,366,293	2,645,303	3,847,770	23,950,110	111,392,590
Total job growth, 1979-89	Percent[3]	-1.2	10.5	17.8	34.3	19.4	5.7	10.6	23.8
Earnings per job, 1989	Dollars[3]	18,570	18,950	18,023	17,603	19,019	17,077	18,444	24,653
Earnings per job growth, 1979-89	Percent[3]	-5.0	-4.0	-8.0	-6.2	-10.6	-5.2	-6.5	.5
Unemployment rate, 1989	Percent[4]	5.5	6.8	6.2	6.6	7.1	8.5	6.6	5.4

[1]Additional demographic and economic statistics can be found in P.J. Cook and K.L. Mizer, *The Revised ERS County Typology: An Overview*, RDRR-89, U.S. Department of Agriculture, Economic Research Service, Rural Economy Division, December 1994.
[2]Table shows 2,276 nonmetro counties, whereas 2,288 are cited in the report. The difference is due to the need to standardize the number of counties for comparisons over time.
[3]Values are calculated from aggregated data.
[4]Values are unweighted county averages.
[5]Values are aggregated dollars (in thousands).
[6]Values are aggregated data.

Source: All measures were calculated by ERS using data from the Bureau of Economic Analysis, the Bureau of Labor Statistics, and the Bureau of the Census.

Best Practices

GEOGRAPHIC LOCATIONS OF BEST PRACTICES



USDA RURAL DEVELOPMENT
LEVERAGED LOAN PROGRAM

Quitman Federal Savings Bank
Bay Meadow Corporation

PARTICIPANT PROFILES

Quitman Federal Savings Bank ("Quitman Federal" or "Association") is a federally chartered mutual savings and loan association with assets of approximately $38.3 million. The Association has only one office, located in Quitman, Georgia, and it has been an integral part of its community since 1936. The Association's strength is residential mortgage lending. As of June 30, 1997, Quitman Federal had a total of $25.6 million in mortgage loans ($22.9 million in permanent loans and $2.7 million in construction loans. The Association also originates a significant number of commercial, real estate, and consumer loans. Recently, the Association has stepped up its community development lending initiatives, particularly in Quitman's downtown historical district.

Bay Meadow Corporation ("Bay Meadow"), incorporated in 1973, is a for-profit real estate development corporation that created a non-profit subsidiary in 1993, in an effort to expand affordable housing opportunities in rural areas. Bay Meadow develops and builds in six counties in southern Georgia and northern Florida. Residential construction, subdivision development, and mortgage originations are the primary business of Bay Meadow, which builds over 30 homes annually.

COMMUNITY BACKGROUND

The primary lending market of Quitman Federal is the Brooks and Lowndes county area, which is located in extreme South Georgia along the Florida border. 1990 census data indicates the combined population of the two counties was 91,379. This area, Lowndes County in particular, has experienced significant population growth. In 1997, the combined population figure for both counties is estimated to be 100,781. The area is expected to be classified as an MSA after the 2000 census.

Brooks County

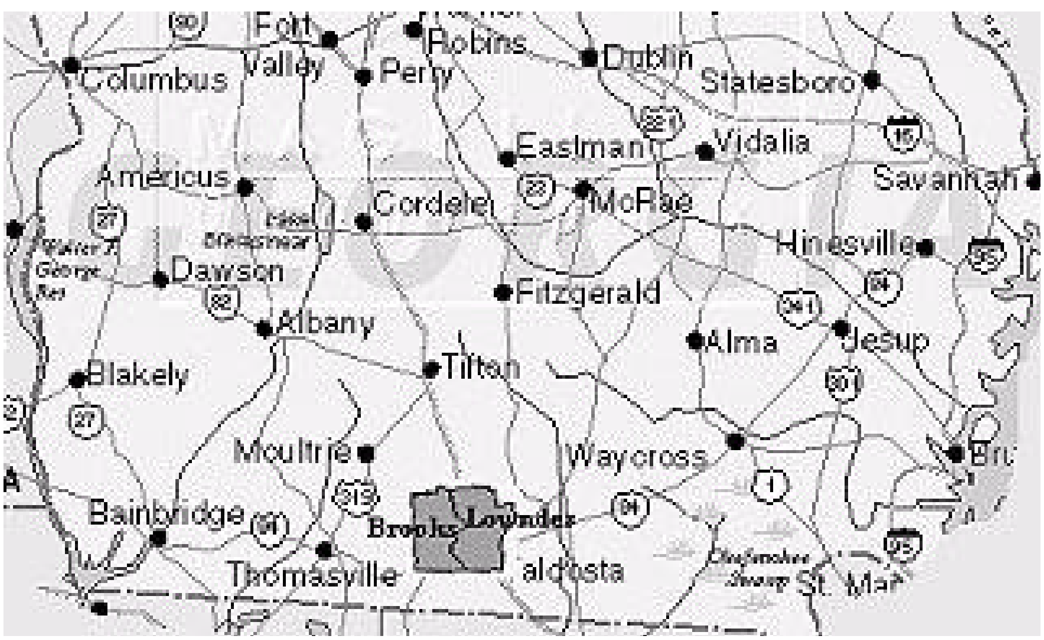
1. Brooks County, which had an estimated 1997 population of 15,868,[1] has grown only modestly since the 1990 census. Brooks County includes the town of Quitman. In 1990, Quitman had a

population of 5,292. Economically, Brooks County couples a mature agricultural industry with a growing commercial and industrial base. Retail trade and service related jobs comprise 60 percent of the county's employment activity. Tourism, primarily hunting and fishing, is beginning to impact the county's economy, which has benefited from the economic growth of nearby Valdosta, Georgia. Brooks County had a median household income of $19,474 in 1990, with an unemployment rate of 4.1 percent. At the end of 1997, the median household income was estimated to be $27,323, indicating an increase of more than 40 percent.

Lowndes County

Lowndes County is the most economically diverse county in south Georgia. As of 1997, Lowndes County's population was 84,913, representing a more than 10 percent increase since the 1990 census. Valdosta, which has generated most of the commercial and economic growth in Lowndes County, is the tenth largest city in Georgia. The service sector has become the county's largest industry, employing approximately 23,312. Manufacturing and farming, while still economically essential to the county, are on the decline. The county's economy has flourished with the recent award of university status to the local four year college, Valdosta State. The university and its more than 9,100 students contribute an estimated $100 million annually to the local economy. Moody Air Force Base, which is located in Lowndes County, has been a big contributor to the local economy since 1940. According to the 1990 census, the median household income was $28,541, and unemployment was 3 percent. Federal Home Loan Bank of Atlanta data indicates that by the end of 1997 the income figure had grown a modest 4.4 percent, to $29,802.

[1] U.S. Census Bureau; "Estimates of the Population of Counties for July 1, 1997, and Population Change: April 1, 1990 to July 1, 1997" published March 17, 1998.



COMMUNITY NEEDS

During the 1990's, Brooks and Lowndes counties experienced an influx of new residents. Many of the people relocating to the area were professionals looking to purchase homes in the high-end sector of the market. Most area lenders focused on this growing market for high-end housing, particularly in Valdosta, and had only marginal interest in making loans for low- and moderate-income single family units. Additionally, because of the demand for high-end housing, the average value of real estate in the area has risen beyond the reach of many low-and moderate-income residents. This was a bitter pill that forced many low- and moderate-income residents out of the home ownership market.

Quitman Federal, one of the few financial institutions in the community to finance low dollar home mortgage loans, sensed the frustration of many low- and moderate-income residents. As an active leader in the community, the thrift recognized the need to increase the level of affordable credit to qualified families or individuals who could otherwise not afford to buy a home.

BEST PRACTICE PROGRAM OR PRODUCT

Quitman Federal has historically operated as a traditional thrift institution, supplying conventional mortgage products and related services to area residents. Two years ago, the thrift was approached by a local developer to provide affordable mortgage financing through the United States Department of Agriculture's ("USDA") Section 502 Rural Development Leveraged Loan Program ("LLP"). This program was developed by the USDA pursuant to Section 502 of the Housing Act of 1949, 42 U.S.C.A. § 1471-1490 (1994 & Supp. 1997) (the "Housing Act"). Although the thrift's management was aware of the LLP, it was not until a meeting with Harold Hagan, President of Bay Meadow, that an alliance was established to use the program to increase home ownership opportunities for local low- and moderate-income residents.

The LLP is administered by the Rural Housing Service, an agency within the USDA. The regulations governing this program are set forth at 7 C.F.R. § 3550.51 to 3550.74 (1997). Under the LLP, up to 100 percent of the purchase price of a home can be financed using two separate loans. One loan is made by a private lender and is subject to market rates and conventional underwriting. The financial institution may finance up to 50 percent of the purchase price of the home. A second mortgage is made directly by the USDA at below market interest rates using the Section 502 Direct Loan Program. In some cases, depending upon the income of the borrower, the interest rate on the second mortgage may be as low as 1 percent. The resulting blended interest rate can make the mortgage very affordable for low-and moderate-income rural borrowers. This arrangement also eliminates the need for the first mortgage lender to obtain private mortgage insurance on the loan while still enabling the borrower to obtain financing for the full purchase price.

The loan amounts and terms that the Rural

Housing Service offers vary depending upon the purpose and amount of the loan. Generally, LLP terms are either 30-year fixed-rate mortgages or 15-year balloon products with a 30-year amortization. Lenders may not use adjustable rate products for the program, nor will the Rural Housing Service consider leveraging arrangements where lender participation is less than 20 percent of the loan amount.

The LLP offers advantages for both lenders and borrowers. For participating lenders the LLP offers the following incentives:

- *The USDA shares the risk on the loan.*
- *The participating lender holds the first position on a mortgage with a very low loan-to-value ratio.*
- *The loans may be sold in the secondary market.*
- *The participating lender may receive CRA credit for making the loan in partnership with the USDA.*

For some borrowers, blending lender loans with the LLP financing may be the only way to make their dream of home ownership a reality. Also, purchasing their home through the LLP may represent their first opportunity to establish a relationship with a private lender. The primary target of the LLP is qualified families in the low- and moderate-income category that do not possess the financial resources required to obtain a conventional residential mortgage. To be eligible for the LLP (i) the borrower's income must be below the median household income for the area; (ii) the borrower must have the intent to purchase and reside in a rural community; and (iii) the borrower must purchase a home that is below the Section 203(b) limits for the area.[2]

[2] The Section 203(b) limits for your area can be obtained by visiting the USDA's website or contacting the USDA office closest to you

EXPERIENCES AND OBSTACLES

Until 1996, Bay Meadow had been a customer of Quitman Federal, primarily through construction and commercial borrowing. At that time, utilizing the LLP initiative, Bay Meadow and Quitman developed a mutual commitment to home ownership opportunities for all community residents and forged an alliance to deliver affordable housing to the area. As indicated above, in order to meet the sponsor/developer requirements of the LLP program, Bay Meadow created a non-profit subsidiary to finance and administer its role in the program, generally consisting of construction and marketing of the homes to low- and moderate-income individuals. To date, all of Bay Meadow's 1998 LLP applicants have been financed by Quitman Federal.

As both the sponsor and developer for the program, the efforts of Bay Meadow are key to its success. Bay Meadow supplies the outreach to and pre-screening of potential home buyers. Outreach generally is achieved largely by word of mouth with some support from modest community advertising. During the initial screening process, Bay Meadow provides various home ownership counseling services. Potential borrowers are pre-qualified and educated about the mortgage process and the responsibilities of home ownership. Moreover, Bay Meadow works as liaison to help Quitman Federal and the borrower identify the appropriate loan products. For lenders like Quitman Federal, one of the challenges of offering innovative affordable mortgage products is understanding both the implications for the borrower and any program requirements that may be imposed for combining nontraditional sources of financing with more traditional mortgage products. Some of those sources might include state or local government assistance progras, church sponsored assistance, or gifts made to the borrower, all of which may be necessary in order to keep the home affordable to a low-income borrower. Bay Meadow has worked with the borrowers and with Quitman Federal to be certain that all parties understand how and why a particular combination of financing sources will work in a particular situation. Quitman Federal's management has indicated that taking the time to fully understand the LLP and its rules is critical to managing an effective low- and moderate- income housing initiative, while mitigating the thrifts exposure to risk.

The methodology used for educating consumers is one-on-one counseling. Bay Meadow's Sales and Marketing Manager Emily Hagan, has indicated that group seminars are not appropriate for many rural consumers because often there are not enough potential borrowers at any given time to justify a seminar and the clients and properties are so unique in each case that an individualized approach is necessary.

As the developer, Bay Meadow has targeted the construction of homes typically in the $65,000 to $75,000 range. Bay Meadow's strategy has been to target their development efforts in existing low- and moderate-income neighborhoods.

Once a house has been constructed, an applicant is selected based upon his or her ability to qualify for the mortgage. For instance, Bay Meadow is currently working with a family of three to purchase a single family home in Lowndes County. The family, with a household income of $18,240, meets the requirements of the program and has been approved for a $73,900 mortgage. Quitman Federal has agreed to make the first mortgage at 20 percent of the loan amount for 15 years at local market rates. USDA Rural Development will finance up to 80 percent of the mortgage for 30 years at 1 percent interest.

Leveraging the LLP Program a family of three purchased the above property for $73,900 in Lowndes County, GA

The down payment and most of the closing costs are built into the USDA Rural Development loan. The borrower is only required to fund the prepaid application expenses, i.e., appraisal fee, credit report fee, earnest money, etc., at closing.

For its efforts, Bay Meadow receives the standard general contractor's fee of 3-5 percent of the purchase price of the home. All Bay Meadow's fees are included in the loan amount. However, Bay Meadow does not derive any fee income for loan originations or its home ownership education program.

Quitman Federal generally takes a 20-25 percent first mortgage position on LLP loans. Additionally, the thrift offers a 15-year mortgage that is amortized over 30 years at local market rates. This product has a 15-year "call feature" that allows the thrift to re-price the loan for the remainder of its term. Quitman Federal management has indicated that this re-pricing feature provides some flexibility for the lender.

CURRENT STATUS

Overall, the LLP has been a very successful initiative for Quitman Federal, Bay Meadow and the community. As of June 30, 1998, the program had made 21 loans totaling $328,891. In 1996, the program's first year, the Association made two loans, and last year a total of 14 loans. To date in 1998, Quitman Federal has made five LLP loans.

Generally, Quitman Federal's LLP loans have performed as well or better than any conventional mortgage portfolio. To date, there have been no loan defaults charged to the program and no delinquencies in excess of 30 days. However, if a borrower should have difficulty paying the mortgage, the program has a series of checks and balances to avoid loan defaults. Much depends on the response and commitment that the borrower has toward repaying their debt. Fortunately, the LLP provides some servicing remedies that are available if a borrower encounters difficulty making payments according to the original arrangement.

The LLP policy recognizes that each lender has an independent responsibility to protect its interest. In the event that the lender determines that the borrower cannot or will not continue to make the payments as agreed, the lender may take action to limit its loss exposure. Taking action usually refers to notifying USDA Rural Development of the status of an outstanding account. If the lender decides to foreclose on an account, USDA Rural Development has a "first refusal" option that allows the agency to buy the entire loan from the lender.

PARTNERSHIPS

Bay Meadow Corporation, USDA Rural Development Leveraged Loan Program.

ADDITIONAL INFORMATION CONTACTS

Quitman Federal Savings Bank
Single-Family Lending
100 West Screven, P.O. Box 592
Quitman, GA 31643
Contact: Mr. Melvin Plair, President
Phone: (912) 263-7538 Ext. 19
Fax: (912) 263-5385

U.S. Department of Agriculture
14th & Independence Ave. SW,
Washington, D.C. 20250
Phone: (202) 720-2791
Main Web Site: www.usda.gov
USDA Facilities Locator: offices.usda.gov
Rural Development Field Offices:
www.rurdev.usda

U.S. Bureau of the Census
Department of Commerce
The Herbert C. Hoover Building
15th and Constitution Ave., N.W.
Washington, D.C. 20230
Phone: (202) 482-2000
Fax: (202) 482-5270
Internet Homepage: http://www.census.gov

ADDITIONAL RESOURCES

The State Data and Research Center
Georgia Institute of Technology
GCATT Building
Room 543
250 14th Street, NW
Atlanta, GA 30318
Phone: (404) 894-9416
Fax: (404) 894-9372
Internet Homepage:
http://sdrcnt.pp.gatech.edu/

Carl Vinson Institute of Government
University of Georgia
201 N. Milledge Ave.
Athens, GA 30602-5482
Phone: (706) 542-2736
Fax: (706) 542-6239
Internet Homepage:
http://www.cviog.uga.edu
GeorgiaInfo Page: http://www.cviog.uga.edu/
Projects/gainfo/contents.htm

Research and Analysis Division
Office of Planning and Budget
270 Washington Street SW
Atlanta, Georgia 30334
Phone: (404) 656-3820
Fax: (404) 656-3828
Internet Homepage:
http://www.opb.state.ga.us/op09000.htm

MULTI-FAMILY CONSORTIA

Community Investment Corporation of North Carolina

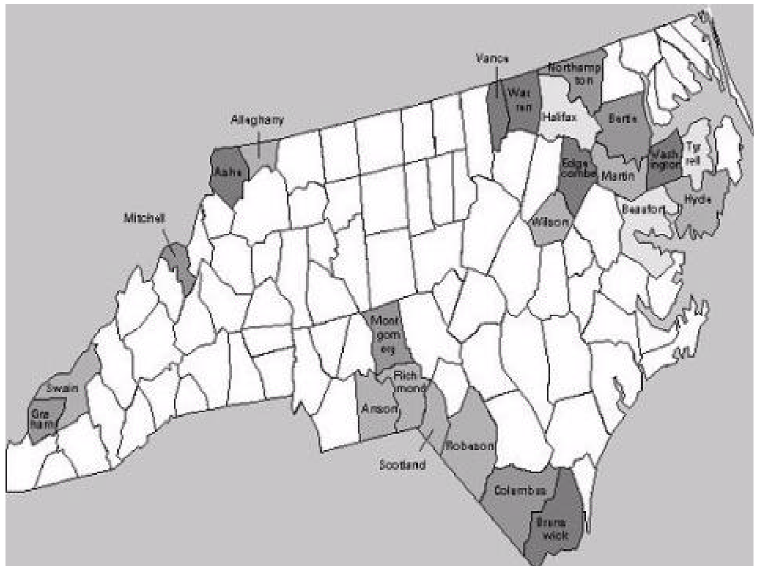
PARTICIPANT PROFILES

The Community Investment Corporation of North Carolina ("CICNC") is a for-profit affordable housing loan consortia formed by the North Carolina Bankers Association ("Bankers Association") as a wholly-owned subsidiary in 1990. It was created to help address housing shortages and the sub-standard conditions of some of the existing housing stock throughout the state. Its primary purpose is to provide long-term financing for the rehabilitation and construction of low- and moderate-income and special needs multi-family housing throughout North Carolina; moreover, CICNC also has an important role as the facilitator of many of its projects by connecting its statewide membership with profit and non-profit developers, community-based project sponsors and governmental agencies that might otherwise never meet.

The initial start-up capitalization for the CICNC was $150,000 and was provided by the Bankers Association. Membership in the CICNC is open to all North Carolina financial institutions. Originally membership consisted primarily of the thrift industry. Today there is broad representation by all types of financial institutions. CICNC currently has 103 member institutions, both banks and thrifts, that include a thrift with assets less than $10 million, as well as some of the largest banks in the state. Consortium membership fees range from $500 to $5,000 and are based on the asset size of the institution. The current capitalization of the CICNC is $280,000.

CICNC operates with an annual budget of approximately $250,000. The consortium employs a two-person staff and shares a support staff and office space with the Bankers Association. CICNC's staff provides critical technical assistance to project sponsors. The CICNC Board of Directors, Executive Committee and loan committees are composed of Chief Executive Officers from the member financial institutions. All projects are owned by limited partnerships or limited liability corporations.

COMMUNITY BACKGROUND



North Carolina consists of three primary geographic regions: Eastern North Carolina, which includes the Atlantic coast and coastal plain areas; Piedmont, which includes the mid-central areas; and Western North Carolina, which includes the Appalachian Mountain areas, both the Great Smoky Mountain and Blue Ridge Mountain chains. Each geographic region, because of its terrain, resource base, and history, has a culture very distinct from the other two. Economically, the Piedmont region is leading the state in most measures of growth. However, the Eastern North Carolina region, boosted by the rapid growth of resort communities in the coastal beach areas, has the fastest population growth in the state. Economic and population growth in the Western North Carolina region has not kept pace with that of the other two regions.[1]

Within these three regions, there are 85 rural counties.[2] The most populated rural counties are in the Eastern North Carolina region while the Piedmont region contains the state's largest urban centers. The North Carolina Office of State Planning estimates that, as of July 1997, 3.8 million residents, or 51.76 percent of North Carolina's total population, were living in these rural counties; while 3.6 million residents, or 48.24% of North Carolina's total population, were living in the remaining 15 urban counties. Based upon 1990 Census Data, these figures represent a 1 percent increase in urban county residents and a corresponding 1 percent decline in rural county residents, indicating a slight shift toward urbanization. More than 40 percent of the rural counties have lost residents to urban centers. North Carolina's rural areas also have lost farms, farm land and farm employment.

Notwithstanding the urbanization trend, 1990 census data show that rural employment grew by 19 percent or 209,000 workers during the 1980s. Forty-one percent of the individuals employed in the state resided in the rural counties. Currently, manufacturing jobs account for 27 percent of all rural employment.[3] However, portions of this job segment (e.g., labor-intensive, low-wage manufacturing jobs) will be particularly vulnerable to the impact of recent trade initiatives. Consequently, the number of manufacturing jobs in North Carolina may decrease significantly in the near future.

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[1] For economic and community development purposes, North Carolina is divided into 7 regions, each of which has a large non-profit regional development commission.

[2] North Carolina Rural Economic Development Center. Economic and Social Trends Affecting Rural North Carolina. November 1992. PP. 9-10.

[3] Ibid.

COMMUNITY NEEDS

In North Carolina, one out of every four families lives in sub-standard housing. Also, it is estimated that an additional 200,000 housing units are needed to address existing housing stock shortages. According to the North Carolina Rural Economic Development Center, 5.1 percent of all occupied housing units in rural counties were classified as substandard in 1990. Multi-family rental units in the rural areas of the state typically fall into two categories, upscale, manicured resort communities or inadequate, poorly maintained properties with no amenities in unsafe neighborhoods. There is a significant need for affordable low- and moderate-income multi-family housing in these communities.

Affordable housing has emerged as a major concern for rural residents nationwide. In rural North Carolina (particularly the resort areas in the mountains or on the eastern coast) rental housing is difficult to find and, if available, very expensive. Demand enables landlords to rent the units for higher prices and on a month-to-month or week-to-week basis. The few year-round rentals that are available are difficult to obtain, since affluent newcomers to the community (professionals such as physicians, attorneys, business owners and wealthy retirees) can afford to pay higher rents. This need for adequate and affordable multi-family housing prompted the creation of the CICNC.

In North Carolina, as in many other states, some rural communities simply do not have local financial institutions with the ability and the desire to finance affordable multi-family housing projects. These projects are often difficult to underwrite and may require many layers of complex financing to make them work. Small, local financial institutions are often not able by themselves to safely originate the loans needed for these projects.

BEST PRACTICE PROGRAM OR PRODUCT

In the 1990's, use of lending consortia has grown significantly, both in the number of participants and the purposes for which they are utilized. Statewide lending consortia provide a multitude of benefits to participating lenders and to the communities they serve throughout the state. Membership in a consortia enables a financial institution to participate in a meaningful way in the financing of community development projects regardless of the size of the project or the asset size of the institution. Risk is controlled not only because there are several participants in the loan, but because experienced multi-family underwriters sit on the loan committee that approves each loan. Importantly for rural communities with few financial institutions, participants in a community development loan, originated by a consortia, receive CRA lending credit regardless of where in the state the actual project is located. Consequently, financial institutions are motivated to participate in loans on projects even though they may be utside their own assessment area.

CICNC financing is available for affordable housing developments throughout North Carolina, including those rural communities that might not have any financial institution presence. Both non-profit and for-profit organizations may apply for CICNC financing. Approved loans are funded by CICNC members utilizing a voluntary loan pool participation process.

CICNC management believes that the only way to develop a similar program in small rural areas is to attract regional or statewide lender participation. CICNC Executive Vice President Roger Earnhardt has consulted on rural consortia models in Georgia and South Carolina and has indicated that a statewide consortium with a rural focus would be plausible because the tax credits and CRA benefits would attract rural as well as large non-rural investors, just as they do in North Carolina.

The Low-Income Housing Tax Credits Program, created as part of the Tax Reform Act of 1986, has played a critical role in the success of all the projects financed by CICNC to date. Developers have been able to use tax credits to generate equity equal to as much as 50 percent of the cost of a project. Financial institutions can help to provide that equity by purchasing the tax credit. The generation of this inexpensive equity is critical to the success of a multi-family project that is designed to house "cost-burdened" renters since the cost of the project nearly always exceeds the value that can be financed by the cash flow of the project. A household is considered "cost-burdened" when it pays 30 percent or more of its monthly income for housing-related costs. The limited cash flow, which is a problem in all affordable projects, is exacerbated in rural areas because the projects are generally smaller and, therefore, unable to reach economies of scale available in larger projects.

EXPERIENCES AND OBSTACLES

The lending process begins with the filing of a loan application with the CICNC. All applications are reviewed by CICNC staff prior to being presented to the CICNC Board of Directors for approval. To be considered, applications must meet the following loan criteria:

- At least 51 percent of the units in a project must provide housing for low-income families that are defined as households with 60 percent or less of the area median income.
- Rent, including utilities, may not exceed the applicable low-income rent ceiling based on 30 percent of the individual household's income.
- The qualified units must be occupied by low-income tenants as long as CICNC financing remains in place.

The approval process for CICNC loans typically takes 45 days from the date an application is submitted. Management indicates that it takes 30 days to assemble all the relevant information, including an appraisal, a market study, preliminary plan design and analysis of the projected operating performance and costs. Generally, within two weeks following the assembly of a complete loan package, it is submitted to the CICNC Board for approval.

Once a loan is approved by the CICNC, a description and analysis of the project is sent to all CICNC members, who are invited to subscribe to a portion of the total loan commitment. The minimum level of lender participation per loan is $10,000. Lenders geographically closest to the proposed project are given a right of first refusal. Typically, this allows local lenders to be a part of projects in their communities, thereby demonstrating their involvement and commitment to the local community in which they do business. An average CICNC loan will have from 20 to 30 participating lenders.

CICNC has financed several rural projects. One example is the Orchard View Apartments in Franklin, North Carolina. This 48-unit affordable housing complex, which was ready for occupancy in November 1, 1994, had total development costs of $2.93 million. Construction financing was provided by the North Carolina Finance Agency and First Citizens Bank of North Carolina. As is typical of affordable multi-family projects, the permanent costs were covered by a combination of equity, loans and grants from a variety of sources including CICNC, Low Income Housing Tax Credits, federal HOME funds, and the Federal Home Loan Bank of Atlanta ("FHLB-Atlanta").

For most multi-family housing projects, CICNC uses a conventional 30-year permanent financing product. The maximum loan-to-value ratio on this product is 75 percent, with a 1-percent fee for an 18-month commitment. The interest rate is fixed for the first 18 years on the 10-year Treasury Note plus a competitive margin. The rate on these loans adjusts in year 19 with a 4 percent lifetime cap and a floor rate of not less than 7.75 percent (the floor rate is subject to change). All loan servicing is done by CICNC using a software program that was designed for lending consortia. The income derived from its servicing activity has helped CICNC become self-sufficient. Lenders receive monthly checks from CICNC for their respective portions of the loan payments. Today this process is routine, although prior to the development of the software, servicing the portfolio was quite challenging.

Securing financing for multi-family housing projects is more difficult for developers in rural communities than in urban settings. Rural communities have fewer banks and a limited number of lenders who are capable of financing multi-family projects. Larger lenders are generally located in urban centers and may be unfamiliar or uncomfortable with lending in rural areas. Also, these lenders may not know the market and are not convinced that a rural project can be profitable. Multi-unit apartments must keep a sufficient number of units occupied to spread the cost of management and maintenance. This is a significant obstacle for multi-family developments in rural communities. CICNC has indicated that the typical rural community apartment project has only 20 to 40 units, often making it necessary for the developer to apply for grants, land donations, seed money or other concessions to cover its costs. In addition, developers can subsidize the low rents and make up for the lack of units over which to spread ase costs by utilizing tax credits.

One of the keys to CICNC's success has been the quality of the technical assistance it provides to the developers who bring the majority of the deals to the table. Having worked on many projects, the staff of CICNC is proficient at assisting the developers in many ways. Certainly, they are able to provide permanent financing, but in addition, they assist developers in grant writing, application filing, coordination of various aspects of the development and identification of other key partners to make a particular development a success. CICNC also has been instrumental in identifying additional sources of funding for developers in rural communities.

Pictured right are the 48 unit Orchard View Apartments, Franklin, NC, which was completed in 1994.

IMPLEMENTATION /CURRENT STATUS

CICNC, which began accepting applications in March of 1991, became a self-sustaining, profitable entity in 1994. Overall, the consortium has funded 68 multi-family projects totaling 3,246 units for $56 million in loans. Of that amount, 34 were rural projects accounting for $26 million in loans. In 1997, CICNC had an active year, closing on 12 developments that produced 525 units for $8.5 million in loans. In addition, CICNC has developed an important relationship with the FHLB-Atlanta.

PARTNERSHIPS

CICNC's housing development initiatives have been accomplished through partnerships with various government agencies in order to achieve the maximum benefit (leverage) from public and private funds designed for affordable housing. All CICNC projects were developed under the federal Low-Income Housing Tax Credits Program. In addition, CICNC developments have utilized CDBG funds, Historic Tax Credits, HUD HOME Funds, Federal Home Loan Bank Affordable Housing Program funds, state housing trust funds and local government housing bonds to subsidize the various projects.

ADDITIONAL INFORMATION CONTACTS

Community Investment Corporation of North Carolina
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Raleigh, NC 27619-1999
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U.S. Bureau of the Census
Department of Commerce
The Herbert C. Hoover Building
15th and Constitution Ave., N.W.
Washington, D.C. 20230
Phone: (202) 482-2000
Fax: (202) 482-5270
Internet Homepage: http://www.census.gov

ADDITIONAL RESOURCES

North Carolina Office of State Planning
116 West Jones Street
Raleigh, N. C. 27603-8003
Phone: (919) 733-4131
Fax: (919) 715-3562
Internet Homepage:
http://www.ospl.state.nc.us/

NC Rural Economic Development Center
4021 Carya Drive
Raleigh, NC 27610
Phone: (919) 250-4314
Fax: (919) 250-4325
Internet Homepage: http://ncredc.org

REHABILITATION LENDING

Kennebec Valley Community Action Program

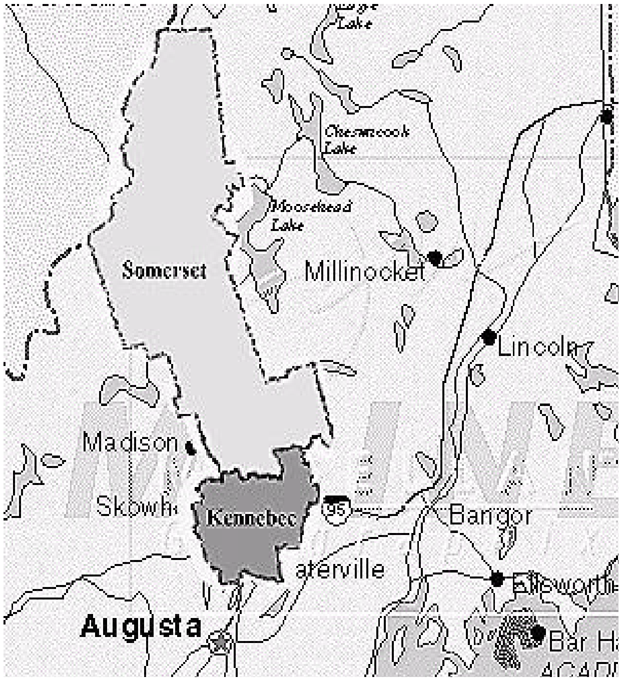
PARTICIPANT PROFILES

Kennebec Valley Community Action Program ("KV Community Action") is a private, non-profit corporation whose mission is to provide social services to low- and moderate-income people and reduce the level of poverty in central Maine. KV Community Action employs more than 200 people and has an annual budget of more than $14 million. Its funding base is diverse and includes support from a variety of federal, state and local agencies, municipalities, and financial institutions, as well as fees paid by clients for services. The Housing Services Department of KV Community Action, which employs 31 people, is composed of three divisions: the Housing Division, the Information Center, and the YouthBuild Program.

The long-term goal of the KV Community Action Housing Services Division ("Housing Services") is to advocate for and help provide safe, affordable housing for low-income residents of Kennebec and Somerset counties. In furtherance of this goal, KV Community Action's Housing Services works in partnership with the Maine State Housing Authority, Kennebec Federal Savings Bank, Consumer Credit Counseling Services, area municipalities, local realtors, area contractors and residents. For nearly two decades, KV Community Action has been providing housing and housing assistance services to the agency's clientele through several educational and lending programs, including: Weatherization, Central Heating Improvement, Housing Preservation, Home Energy Assistance, Home Ownership Training, Families in Transition, Affordable Housing, Training and Technical Assistance, and Fix-Me Home Repair, the best practices focus of this section.

COMMUNITY BACKGROUND

KV Community Action's service area includes all of Kennebec and Somerset counties in Maine. These two counties cover a large, essentially rural region of 80 cities, towns, and plantations, as well as a large section of uninhabited forest land. The region has a population of nearly 166,000 people scattered across 4,795 square miles, resulting in low population density and dispersed settlement patterns. Approximately 90,000 people, or nearly 56 percent of the region's total population reside in the 10 largest communities in KV Community Action's service area.



Within the service area, population pockets range from a low of 36 people to a high of 21,235. The service area's overall population density of 34.5 persons per square mile, quite low relative to the urbanized northeast, with a population density average of 317.9 persons per square mile, masks the fact that most of the population of Kennebec and Somerset counties is located in communities along Interstate 95. Less than half the population resides in the smaller towns and on plantations.

Manufacturing industries, such as lumber, paper, and textiles, dominate the region's economy. However, the industry has been on the decline, dropping 14 percent in the last decade. Conversely, the service industry has increased 23 percent over the same 10-year period. Most of this growth has occurred in health care, home care, and tourism.

Mirroring state and national trends, the population of the KV Community Action service area is an aging population. The median age of the population in Kennebec and Somerset counties increased from 30.6 years in 1980 to 34.1 in 1990. The KV Community Action two county service area had 19.4 percent of its population in the 45- to 64-year-old age bracket in 1990, with 13.3 percent age 65 or older. 1993 U.S. Census Bureau estimates confirm that the service area population continues to age, with residents in the 45- to 64-year-old bracket totaling 21.8 percent of the population, 36,836 individuals, and those in the 65 or older bracket representing 13.8 percent of the population, 23,302 individuals. Further, Maine's median household income in 1993 was estimated at $28,732. The median household income for Somerset County in 1993 was estimated at only $26,178, while Kennebec County was higher, slightly surpassing the state median, at $32,776.

COMMUNITY NEEDS

Generally, the housing stock in Maine is very old and, in many cases, in very poor condition. According to the 1990 census, Maine's housing stock, 291,401 units, was the seventh oldest in the nation, with 39 percent built before 1939 and 50 percent before 1960. In KV Community Action's two county service area, 35 percent of the housing stock was created prior to 1939, and 49 percent predates 1960. The key to sustaining the quality of the existing housing stock is maintenance, repair, and selected replacement. Over time, however, this involves substantial cost to the homeowner.

A critical factor in dealing with the older housing stock is the safety of electrical, plumbing, water, waste disposal, and structural components. The current condition of many of these components creates hazards for the homeowner. The threat of fire is of special concern to low-income homeowners because older heating systems are often inadequate or poorly maintained and thus, dangerous. Considering that the mechanical and structural life of most homes ranges between 15 and 30 years, a large number of these homes are in need of major rehabilitation.

Low- and moderate-income individuals trying to obtain funds to rehabilitate, repair, or make their homes more livable have found very few alternatives. Those who can afford only small payments for home improvement loans often do not qualify for conventional products.

BEST PRACTICE PROGRAM OR PRODUCT

The Fix Me Loan Program ("Loan Program") is a low-interest rehabilitation loan program funded by the state and specifically targeted to low-income homeowners. The mission of the Loan Program is to make loans to low-income households for home improvements and, thus, help improve the existing housing stock throughout Maine.

Homeowners may borrow as little as $500 or as much as $15,000 to make necessary repairs to their homes. Terms of the loans are for up to 15 years to enable low-income borrowers to make affordable monthly payments with interest rates as low as 2 percent.

The Loan Program is administered separately by 11 Community Action Program ("CAP") agencies, including KV Community Action, under contract with the Maine State Housing Authority. Although the CAP agencies that administer the Loan Program may have different methods of marketing and processing the loans, the delivery of the product is basically the same. All loans are originated and closed by the CAP agencies and sold to the Maine State Housing Authority (“Housing Authority”).

The Loan Program is a self-sustaining, fee-based operation. The administrative costs of the Loan Program are funded by two primary sources: loan origination fees and project management fees. The loan origination fee is either $300 or $500 and the project management fee is a percentage of the loan amount, ranging from 0 percent to 8 percent, depending upon the complexity of the rehabilitation to be financed. All fees are paid by the borrowers and are usually included in the loan amount. The fees are properly disclosed in the Truth In Lending Statement, which is prepared by the CAP agency. The Housing Authority, which serves as a secondary purchaser of all the Loan Project loans, periodically adjusts the origination and project management fee structure.

The Housing Authority has established two below-market interest rates for program borrowers. Currently, the rate on the rehabilitation loans is either 2 or 4 percent. In order to be eligible for the 2 percent rate, the rehabilitation project must, at completion, meet the “Housing Quality Standards” established by the U. S. Department of Housing and Urban Development ("HUD").

These standards are set forth in 24 C.F.R. § 982.401 (1997). If the finished project does not meet HUD's Housing Quality Standards, the borrower will receive an interest rate of 4 percent.

KVCAP Fix Me funds were used to expand this home by adding an additional unit and frost wall. The total cost of the project, located in Kennebec County, ME was $15,000.

Experiences and Obstacles

KV Community Action handles all loan closings in-house, thereby reducing expenses. Most types of home repairs, including those to heating systems, septic tanks, wells, roofs and interior renovations, can be done under this loan program. Throughout the rehabilitation, the project manager works closely with the borrower to address any issues or concerns. All payments for the materials and the services of the contractors are made from an escrow account at KV Community Action, which is established for each Loan Program borrower with funds received from the Housing Authority and maintained at Kennebec Federal Savings Bank. KV Community Action pays the contractor from the escrow account as each phase of the project is completed. When the rehabilitation project is completed and the funds have been disbursed, arrangements for loan servicing are contracted through the Housing Authority.

One challenge for KV Community Action in its efforts to assist low-income homeowners in upgrading their homes to acceptable health and safety standards has been the successful promotion of the program. This is due to the size and rural nature of the community being served by KV Community Action, which covers nearly 500 square miles. In some cases, remote towns are located as much as 100 miles from the KV Community Action office. KV Community Action has addressed this problem through community outreach efforts and newspaper and radio advertisements. The Housing Authority also remains active and supports KV Community Action by assisting with the marketing of the program. Their combined efforts have helped ensure community awareness of the program.

Current Status

The Loan Program is in its third year of operation. During this period, KV Community Action has facilitated nearly 400 loans in the Kennebec and Somerset areas. The Loan Program has provided $3.8 million in rehabilitation financing to date, with all of the loans going to households having incomes less than 80 percent of the state's median income. Statewide the program has a default rate of 8 percent. KV Community Action management attributes the success of this program to the efforts made to make a loan truly affordable for low-income borrowers. The low payments enable these homeowners to rehabilitate their homes and repay their debts on schedule.

Partnerships

KV Community Action's Housing Services Department works in partnership with the Housing Authority, Kennebec Federal Savings Bank, Consumer Credit Counseling Services, area municipalities, local realtors, area contractors, and residents in the development of the affordable housing activities within each town or locale.

Additional Information Contacts

Kennebec Valley, C.A.P. Agency
Rehabilitation Lending
101 Water Street
Waterville, ME 04903
Contact: Ms. Nancy Findlan, Housing Director
Phone: (207) 873-2122
Fax: (207) 873-0158

U.S. Bureau of the Census
Department of Commerce
The Herbert C. Hoover Building
15th and Constitution Ave., N.W.
Washington, D.C. 20230
Phone: (202) 482-2000
Fax: (202) 482-5270
Internet Homepage: http://www.census.gov

Additional Resources

Aaron Shapiro, Program Manager
Community Development Block Grant Program
Office of Community Development - State of Maine
Phone: (207) 287-8485
Fax: (207) 287-8070

Center for Business and Economic Research
School of Business
University of Southern Maine
118 Bedford Street
Portland, ME 04104-9300.
Phone: (207) 774-9891; (207) 780-4187
Fax: (207) 780-4046
Internet Homepage:
http://www.usm.maine.edu/~cber/

Energy and Housing Services
Maine State Housing Authority
353 Water Street
Augusta, ME 04330-4633
Contact: Mr. Peter Wintle, Director

SELF-HELP HOUSING

Farmers and Mechanics National Bank
Interfaith Housing of Western Maryland

PARTICIPANT PROFILES

Farmers and Mechanics National Bank ("F&M" or "the Bank") is a subsidiary of F&M Bancorp, the fourth largest Maryland based independent bank holding company. F&M's main office is located in Frederick, Maryland. The Bank has approximately $799 million in assets and operates 24 full-service community branches in Frederick, Montgomery, and Carroll counties in Maryland.

F&M offers electronic banking options throughout its market, including personal and business PC banking access and 24-hour banking. In addition to being a market leader in commercial and retail banking, F&M has a strong commitment to the local community. Through its CRA Department, F&M offers assistance to low- and moderate-income customers through a variety of services and products.

F&M has assisted first-time home buyers through its Afford-A-Home 100-percent financing program. The Bank also supports the Housing Opportunities Commission in Montgomery County by aiding borrowers with down payments and closing costs. Key Alliance, the newest division of F&M's Trust and Investment Management Group, provides free financial planning services to customers with no minimum income or investment requirements. Finally, F&M is a Small Business Administration lender and makes loans to many local businesses.

Interfaith Housing of Western Maryland ("Interfaith Housing") focuses on rural housing needs in the five westernmost counties of Maryland. It was founded in 1989 by regional religious and lay leaders who are committed to improving the housing conditions for the poor. Since 1992, Interfaith Housing has developed 19 projects representing more than 380 units. The projects include rental housing for seniors, single family homes for very low-income purchasers, and shelters for domestic violence victims.

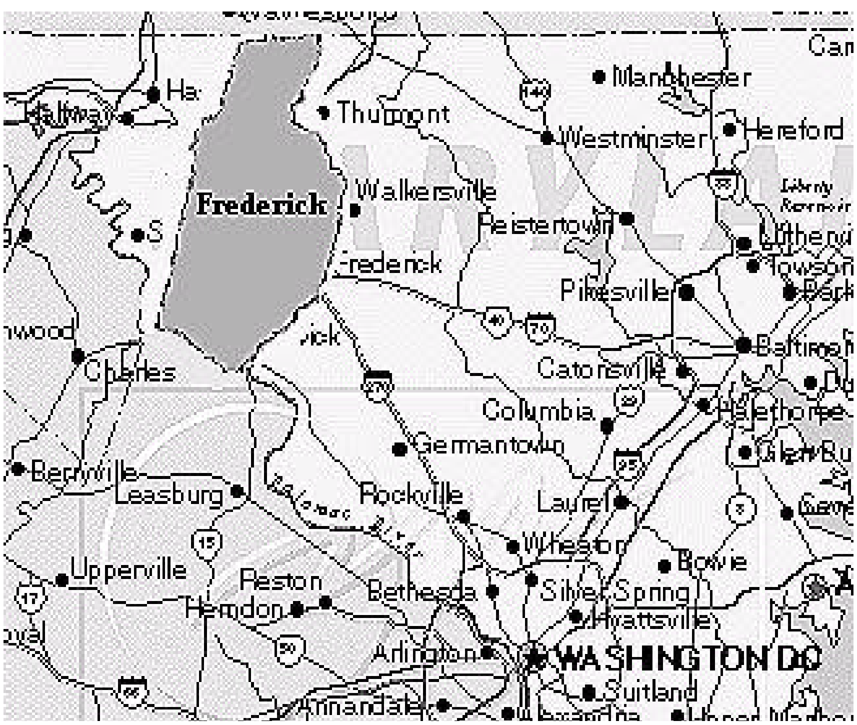
F&M and Interfaith Housing have joined forces on various initiatives to create affordable housing throughout Frederick County since 1993. Although F&M and Interfaith Housing are not in a formal partnership with one another, they have developed a strong business relationship with the common goal of creating affordable housing in western Maryland.

COMMUNITY BACKGROUND

Frederick County, the second largest county in Maryland, is located 50 miles northwest of Washington, D.C. Historically, Frederick County residents have been employed in the farming and manufacturing businesses. The county encompasses 428,197 acres, of which approximately 280,223 acres, or 65.5 percent, are devoted to agricultural and rural uses.

Over the last decade, Frederick County has experienced a steady increase in population. According to the Maryland Office of Planning, the county's population increased from 150,208 in 1990 to 175,399 in 1995. By the year 2000, it is estimated that the population of Frederick County will exceed 203,000 people. Because of the population increases, Frederick County also has seen a slow but continual growth in commercial and residential development. Residential development efforts have primarily concentrated on single-family residences. Developers built 12,698 housing units between 1980 and 1990, of which 10,534 were single-family units. Between 1991 and 1997, new housing units totaled 13,406, 11,612 of which were single family units.

The county is home to Fort Detrick, a military base that employs 4,700 people and serves as the county's second largest employer, surpassed only by the county government itself. The county's median family income in 1997 was $50,700, and the unemployment rate is at 3 percent. Economically, the area is becoming more diversified to meet the needs of a growing population. Farming and manufacturing are still important industries in the area, but service related business is growing rapidly.



COMMUNITY NEEDS

The high cost of housing to rural families located outside of the metropolitan Washington, D.C. area has virtually excluded many low- and moderate-income borrowers from the housing market. The primary identifiable barrier to affordable housing in Frederick County is the cost of development, which is exacerbated by the extremely high cost of land. The latter is a result of the proximity of Frederick County to Montgomery County, one of the most expensive counties in America in which to live. As a result of the high costs of housing, many rural families cannot save sufficient funds to cover the down payment and settlement costs.

BEST PRACTICE PROGRAM OR PRODUCT

In their most ambitious housing initiative to date, F&M and Interfaith Housing worked together to develop Mountain View Community Homes ("Mountain View"), a 22 home single-family residential development for low- and moderate-income residents in Brunswick, Maryland. A new strategy was utilized to secure the property and build the homes. This strategy involved the participation of the low- and moderate-income buyers and became known as the Self-Help Program.[1] Through this program, families are able to trade roughly 1000 hours of volunteer effort for cash and equity in their homes**.** Mountain View is the region's first housing development of this kind.

The Mountain View project began in February 1995 when Interfaith Housing identified a site for development that had originally been considered for the construction of a school. Although the foundation for the school had already been laid, the site was abandoned making the property available for purchase. F&M made a $350,000 secured real estate loan to cover the acquisition costs for the parcel of land. F&M evidenced its strong support for the project and for Interfaith Housing by financing 100 percent of the appraised value of the property. Also, during the course of the Mountain View development, F&M competed for and won $73,500 in self-extinguishing funding from the Federal Home Loan Bank of Atlanta ("FHLB-Atlanta"). The direct FHLB-Atlanta subsidy was passed through to Interfaith Housing to help cover the extensive site development costs on the parcel of land.

A key component of the Self-Help Program called for the qualified home buyers to contribute sweat equity to help build their homes. The sweat equity was utilized to cover two-thirds of the labor necessary to construct the homes, thus reducing the mortgages by a range of $8,000 to $15,000. With the borrower's sweat equity and FHLB-Atlanta subsidies in place, the loan amount financed for the homes in Mountain View ranged between $84,000 and $104,000. However, the appraised value of the home upon completion of construction ranged between $95,000 and $123,800. Therefore, at closing, each of the new borrowers had equity in their properties in an amount equal to what is seen in more conventional financing arrangements.

The household incomes of the families who have qualified for the Self-Help Program ranged between $12,000 and $40,000. To assist those families who qualified, but lacked sufficient funds to cover the down payment and closing costs, Interfaith Housing utilized the U. S. Department of Agriculture's Rural Housing Services 502 Loan Program ("502 Program"). This is a direct loan program, as opposed to a guarantee program, which features low interest rates and no down payment requirements. Use of the 502 Program enabled these borrowers to afford the homes being developed by Interfaith Housing, despite their low incomes.

The outreach, pre-qualifications, budget and credit counseling, and home ownership education workshops were administered by Interfaith Housing. Interfaith Housing developed its own Self-Help Program to administer the training requirements and provide adequate pre-construction training. As part of the requirements, the families participated in a minimum of 25 hours of pre-construction classroom training and 30 hours of on-the-job site training.

Pictured above is the Mountain View Project's second building group at work. The project, which was financed by FMNB, was completed in January 1998.

Through the Self-Help Program, the selected applicants were placed into three "building groups" that were trained sequentially to meet the time frames needed to acquire their lots and build their homes. Members of each building group served on construction teams to build all of the homes for their group. The construction teams worked under the direction of an Interfaith Housing construction supervisor. The families worked between 800 and 1300 hours to complete their group's homes. The construction of each group of homes generally required between 8 and 12 months.

[1] Schnell, Susanne C. Profiles of Partnership Achievements: Street Tested Strategies for Strengthening Neighborhoods. The Social Compact. 1997. P. 64.

EXPERIENCES AND OBSTACLES

The site originally purchased by Interfaith Housing presented some obstacles because it included the foundation of the school, which needed to be removed, and it had areas that were potentially unsuitable for housing development because of the hilly terrain. F&M extended credit to Interfaith Housing knowing that some of the lots could not be developed. Further, F&M management understood that non-profit developers are often forced to purchase land that might be considered unsuitable for housing development by the private sector because the land is affordable. In the case of the Mountain View project, two of the lots purchased by Interfaith Housing could not be developed for housing.

F&M found it helpful to issue letters of credit to the local municipality on behalf of the Program's borrowers. The letters of credit were needed, as a bond, before the municipality would approve infrastructure development such as sidewalks, gutters, water, and sewage drains. The bond is generally required by all municipalities to ensure that the community infrastructure is developed according to local codes.

The demand for the housing was so great that F&M agreed to finance the acquisition of a second parcel of land. The land was used to develop five additional lots in Brunswick. A follow-up loan of $95,000 was settled in September 1996 to fund the acquisition and development of the five lots. Those lots were financed at 90 percent of acquisition cost, with flexible underwriting. F&M's loan was repaid from normal sales activity in May 1997.

CURRENT STATUS

To date all of the Mountain View lots have been sold and the construction of the homes has been completed. The first seven borrowers moved into their new homes in January 1997. Another 10, from the second building group, moved into their homes in October 1997. The remaining five homeowners recently occupied their homes in January 1998. As part of the Self-Help Program, Interfaith Housing conducts post-purchase counseling workshops. To date there have been no defaults on the mortgages.

Because of the success of the Self-Help Program, F&M agreed to provide interim pre-construction loans and grants for two additional affordable housing developments. Weinburg House, located in Frederick, Maryland, provides 23 affordable multi-family units for seniors 62 or older and/or handicapped residents with incomes between $11,000 and $26,340. The apartment complex features an elevator, wall-to-wall carpeting, individually controlled heat and air conditioning, and rent of $320 per month. Additionally, Weinburg Knolls, located in Woodsboro, Maryland, will provide 14 affordable three and four-bedroom single family, detached homes for families earning between $20,000 and $32,000 (for a family of four). Construction of the infrastructure is scheduled to begin in February 1998.

PARTNERSHIPS

Interfaith Housing of Western Maryland, (sponsorship, outreach), Federal Home Loan Bank of Atlanta, (Subsidies; Land Purchases), USDA Rural Housing Services, (502 Low Interest Rate Mortgage Program), County of Frederick (Affordable Housing Council Grant), State of Maryland, Dept. of Housing and Community Development (Low Interest Rate Mortgages).

Additional Information Contacts

Farmers and Mechanics National Bank
Self-Help Housing
110 Thomas Johnson Drive
Frederick, Maryland 21702
Contact: Mr. Jody Yee
CRA Officer
Phone: (301) 694-4121
Fax: (301) 695-3080

U.S. Department of Agriculture
14th & Independence Ave. SW
Washington, D.C. 20250
Phone: (202) 720-2791
Main Web Site: www.usda.gov
USDA Facilities Locator: offices.usda.gov
Rural Development Field Offices:
www.rurdev.usda

Additional Resources

Maryland Office of Planning
301 West Preston Street
Baltimore, Maryland 21201
Phone: (410) 767-4500
Fax: (410) 767-4480
Home Page: http://www.op.state.md.us/

Maryland Department of Housing and Community Development
100 Community Place
Crownsville, Maryland 21032-2023
Phone: 1 (800) 756-0119; (410) 514-7700
Internet Home Page:
http://www.dhcd.state.md.us/

FIRST-TIME
HOMEBUYER PROGRAM

Glacier Affordable Housing Foundation
Glacier Bank

PARTICIPANT PROFILES

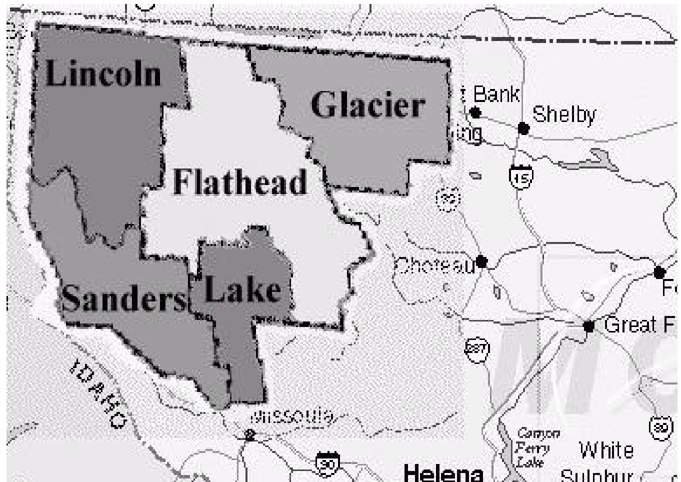
Glacier Bank is a state-chartered savings bank with assets of approximately $365 million. The Bank was chartered in 1955 and has a dominant presence in western Montana. Glacier Bank is a wholly-owned subsidiary of Glacier Bancorp, Inc. ("Bancorp"), which also owns Glacier Bank of Whitefish, Glacier Bank of Eureka and First Security Bank of Missoula. Glacier Bank has 13 offices located primarily in small rural towns in northwest Montana.

Glacier Bank has a significant commercial loan portfolio. However, it also makes home mortgage loans and consumer loans, and has aggressively offered and promoted a free checking program. In addition, the Bank is an active participant in government loan programs and it typically originates one-third of its real estate loan volume in FHA, VA and U.S. Department of Agriculture ("USDA") Rural Development loan programs. For example, in 1997, Glacier Bank was recognized by USDA Rural Development as the number one rural development lender in the state of Montana. Glacier Bank also has the distinction of being one of the first financial institutions to participate in the FHA's 184 pilot project for making loans on tribal lands.[1] Also, the bank is among the top SBA lenders in the state.

Glacier Affordable Housing Foundation ("the Foundation") was established by Glacier Bank in 1995 as a separate non-profit organization to provide down payment and closing cost assistance to low- and moderate-income first-time home buyers. The Foundation applies for grants that are leveraged with private funds to provide affordable housing in high cost rural areas of northwest Montana. The Foundation, although established by Glacier Bank, is governed by its own separate board of directors.

[1] The purpose of this project is to provide access to sources of private financing to Indian families, Indian housing authorities, and Indian tribes, who otherwise could not obtain housing financing because of the unique legal status of Indian lands and lack of access to private financial markets.

COMMUNITY BACKGROUND



Glacier Bank's primary lending market is northwest Montana and includes the counties of Flathead, Lake, Lincoln, Sanders and Glacier. As of the 1990 Census, the population of this five-county region was 118,530. The Montana Department of Commerce estimates that as of July 1, 1997, the population in these counties had climbed to 137,760. The median income for the area in 1993 was $23,642. According to June 1998 Montana Department of Commerce data, the region suffers from an unemployment rate of 9.6 percent. Almost 20.3 percent of the region's population lives below the national poverty level.

This area has a diversified economic base composed of wood product harvesting, primary metal manufacturing, mining, energy exploration and production, agriculture, high-tech related manufacturing, and tourism. Tourism is heavily influenced by the area's close proximity to Glacier National Park, which has in excess of 1.5 million visitors per year. The Big Mountain Ski Areas and Flathead Lake, the largest natural body of fresh water west of the Mississippi River, also attract a large number of visitors.

COMMUNITY NEEDS

Many people have found the clean air, lakes, skiing and other amenities of northwest Montana very appealing and are willing to pay higher prices for housing to live there. The real estate market escalated in response to this demand and many of the existing residents, particularly those of low- and moderate-income means, are now unable to afford their dream of home ownership. The Foundation's Chairman observed that prior to its creation no one was prepared to address the affordable housing crisis in such a rural area. Even government programs with minimal down payments could not help the low and moderate-income home buyers because monthly mortgage payments were still unaffordable. Income in Glacier Bank's market area has not kept pace with the rising costs of homes.

BEST PRACTICE PROGRAM OR PRODUCT

As noted briefly above, Glacier Bank's response to these problems was the establishment of the Foundation.[2] The idea for the Foundation originated with the manager of the Bank's real estate department who proposed that Glacier Bank establish an affordable housing foundation that would apply for grants and make those funds available to first time home buyers increasing their down payment so that the monthly mortgage payment would be manageable. It was also envisioned that the Foundation should be able to share in any upside that the families realized through the eventual sale of these properties that were acquired with this generous assistance.

It took several months for the Foundation to be designated by the Internal Revenue Service as a tax-exempt organization under Section 501(c)(3) of the Internal Revenue Code, but approval was finally obtained in the fall of 1995. In the interim, Glacier Bank applied for and obtained a $610,000 grant from the Federal Home Loan Bank of Seattle to fund the initial operation of the Foundation. This money was used as matching funds for additional HUD Community Development Building Grants and HUD HOME grants to the counties served by the Bank, the first time all of these counties had an opportunity to participate in solving an affordable housing problem.

With a loan of $26,714 from the Glacier Affordable Housing Foundation, a family of two was able to purchase the above home in Flathead County, MT.

To be eligible for assistance from the Foundation, borrowers are required to satisfy four requirements: (i) stable employment, (ii) income that is less than 80 percent of the area's median income, (iii) acceptable credit history, and (iv) completion of a 9-hour First-Time Home Buyers Course sponsored by the Foundation at a local college. The Foundation's organizers and operators feel strongly that education is critical to the long term success of their operation. The courses are customized by using local builders, realtors, credit bureaus and loan officers of the Bank to teach the program.

The Foundation provides second mortgages at zero percent interest and no monthly payment. These funds, which generally range between $15,000 and $25,000, are combined with the borrower's funds, 1 to 2 percent of the sales price, to make up the down payment on the home. Sometimes borrowers who are not able to provide the 1 to 2 percent required down payment can donate sweat equity to the transaction in lieu of funds. The Foundation's funds do not need to be repaid until the property is sold. At that time, the borrower must repay the Foundation's second mortgage, together with a percentage of the appreciation on the property, to ensure that sufficient funds are available for use by the next low-income borrower.

In 1996, the Foundation was able to leverage the grant funds received and assist a larger number of low- and moderate-income residents when the Montana State Board of Housing ("Housing Board") agreed to purchase up to $5.5 million in 30-year fixed rate first mortgages at substantially below market rates. The interest rates ranged from 5.5 percent to 6.5 percent, depending on the income category of the borrower. Three of Bancorp's subsidiary banks, Glacier Bank, Glacier Bank of Whitefish and Glacier Bank of Eureka, each agreed to originate the loans and service them for the Housing Board. The Housing Board and the Bancorp banks also agreed to reduce their fees by half to make the program even more affordable. Community outreach to the borrowers was administered by Northwest Montana Human Resources, Inc., a local non-profit agency.

The combination of low interest rate first mortgages and the down payment assistance provided by the Foundation served to create a home buyer's program that truly meets the needs of this community. With no monthly repayment required until the property is sold, and with the very low interest rate provided by the long-term financing, many homeowners' mortgages are lower than what they previously paid in rent.

[2] For a discussion of the various types of foundations, readers may access the document titled "Types of Foundations" at the Council on Foundations website at **www.cof.org/basics/types.html**. The legal definition and essential elements of a community foundation is covered in the electronic document titled "Legal Definition of a U.S. Community Foundation" at the Council on Foundations website at **www.cof.org/community/legaldef.html**. The Council on Foundations website contains an extensive collection of useful information on Foundations.

EXPERIENCES AND OBSTACLES

In October, 1996, after the necessary capital, partnerships and legal documentation were in place, the Foundation began making loans to low-income, first-time home buyers. The first loan closing was a big event attended by most of the partners in the Foundation, including the Federal Home Loan Bank of Seattle, the Housing Board, and Tony Hernandez, the Assistant Secretary, from the Denver office of HUD. Response to the program was so enthusiastic that the Foundation had to hold a lottery to choose its first home buyers.

One of the most significant undertakings for the Foundation was the extensive amount of training necessary for all parties involved in the process. It began with the first-time home buyers, and extended to the mortgage loan officers, loan processors and closers, and realtors. This was a large task because it had to be done in each of the five counties being served. The Foundation was able to structure a nine hour first-time home buyer course through a local college, which was extended into each of the marketing areas. This was the first time that residents in these communities had ever received formal training in purchasing and maintaining a home. The Foundation strongly believes that a comprehensive home ownership education is one of the major components to a successful affordable housing program.

The single most critical ingredient in the success of the Foundation was the level of cooperation from the program's varied partners. Each partner was able to bring a specialization to the process and was willing to do what was needed to ensure that the Foundation met its objectives. For instance, Glacier Bank housed the program and provided home ownership counseling, while the Northwest Montana Human Resources Center provided marketing and outreach and the Housing Board created a secondary market for the low interest rate loans. No one entity acting alone could have accomplished these goals.

CURRENT STATUS

To date, the Foundation has received a total of $2.1 million in grant funds. By the end of 1997, the Foundation had assisted 69 low- and moderate-income borrowers, and, impressively, 85 percent of them earn less than 70 percent of the median income for the area. More than half of these borrowers earn less than 60 percent of the median. To date, first-time home buyers have purchased homes worth $4.7 million, for which the Foundation has provided down payment and closing cost assistance totaling $1.1 million. The Foundation's goal with its existing grant funds is to assist approximately 150 families. The program appears to be working as envisioned. The payment histories on the first mortgages in the program have been excellent, indicating that the financing as structured really is meeting the needs of these low- and moderate-income families, many of which are single parent households.

PARTNERSHIPS

The Foundation has grown into a large partnership that includes the Federal Home Loan Bank of Seattle, the Federal HOME Investment Partnership Program and the Community Development Block Grant Program, the Department of Housing and Urban Development, the Rural Housing Services (502) program, the City of Kalispell, the county commissioners of Flathead, Lake, Lincoln, Sanders and Glacier counties, the Ronan Public Housing Authority and Northwest Montana Human Resources, and the Housing Board.

ADDITIONAL INFORMATION CONTACTS

Glacier Affordable Housing Foundation
c/o Glacier Bank
P.O. Box 27
Kalispell, Montana 59903
Contact: Mr. Steve Van Helden, Executive Vice President
Glacier Bank
Phone: (406) 756-4253
Fax: (406) 756-4204

ADDITIONAL RESOURCES

Census & Economic Information Center
Montana Department of Commerce
1424 Ninth Ave
P.O. Box 200501
Helena, Montana 59620-0501
Phone: (406) 444-2896
Fax: (406) 444-1518
Internet Home Page:
http://commerce.state.mt.us/ceic

Housing Division
Montana Department of Commerce
836 Front Street
Helena, MT 59601
Phone: (406) 444-3040
Internet Home Page:
http://commerce.state.mt.us/housing/index.htm

The Foundation Center
79 Fifth Avenue/16th Street
New York, NY 10003-3076
Phone: (212) 620-4230
or (800) 424-9836
Fax: (212) 807-3677
Internet Home Page: http://fdncenter.org

Join Together
441 Stuart St.
Boston, MA 02116
Phone: (617) 437-1500
Fax: (617) 437-9394
Internet Home Page: www.jointogether.org
Gopher Site: gopher://gopher.igc.apc.org:7003

Council on Foundations
Human Resources Department
Reference No. 217
1828 L Street, NW, Suite 300
Washington, DC 20036
Phone: (202) 466-6512
Internet Home Page: http://www.cof.org

Central Appalachian Peoples Federal Credit Union

PARTICIPANT PROFILES

The Central Appalachian Peoples Federal Credit Union ("Credit Union") is a federally-chartered, member-owned credit union, whose members either live in the Appalachian region of Kentucky or in some way assist in its community-based economic development. Non-profit members located outside the Credit Union's region may request services if their mission is compatible with that of the Credit Union. The Credit Union began operating in 1980 with one office, 13 members, and $65 dollars in capital. As of mid-1997, the Credit Union has three branches, 2,000 members, and total assets of $5 million. Members of the Credit Union, most of whom are low-income workers, are provided with savings account services and loans

Since 1980, the Credit Union has made more than 7,700 loans totaling $15 million dollars. Half of these loans were made to members earning less than $12,000 a year; 75 percent to members earning less than $18,000 a year. 60 percent of the loans were made to women and approximately 20 percent of the loans were made to individuals receiving some form of federal transfer payments, such as Aid to Families with Dependent Children, Social Security benefits, or food stamps.

In addition to the Individual Development Accounts ("IDA") that represent the Best Practice that is the focus of this section, the Credit Union has participated in a number of other programs to assist low- and moderate-income persons in its market area. In 1994, the Credit Union, the Human/Economic Appalachian Development Corporation, and the Federation of Appalachian Housing Enterprises Incorporated established the Appalbanc Community Development Financial Institution ("Appalbanc"). Its primary mission is to promote individual and community development in rural central Appalachia, and is backed by combined assets of $20 million. In partnership with more than 70 community-based development organizations, Appalbanc is successfully changing some of the fundamental realities of rural poverty by providing access to home mortgages and small business and consumer loans for low- and very-low income people.

The Credit Union is expanding its mortgage lending programs. During 1996 and 1997, the Credit Union effectively used the Federal Home Loan Bank of Cincinnati's Affordable Housing Program to obtain $800,000 in grants to subsidize very low-income housing. The Credit Union is one of the few originators of HUD FHA/VA guaranteed loans in the region. Its secondary market-driven products include those offered by Rural Housing Services, State Housing Agencies, and Fannie Mae.

COMMUNITY BACKGROUND

The Credit Union's primary market area is a 23 county region of Appalachian Kentucky. This is a chronically low-income area where the median household income ranges from $8,600 to $13,200. According to the Kentucky State Data Center, in 1990, the 23 counties served by the Credit Union had poverty rates between 20.6 percent and 46.4 percent, compared to the national poverty rate of 13.1 percent.

Central Appalachia also has one of the highest rates in the country for undereducated adults. A recent study by the Appalachia Research Center at the University of Kentucky noted that the 49 Appalachian counties of Kentucky had an illiteracy rate of 48 percent; the highest level in the nation.

Owsley County, the site of the IDA program, is a geographically small county in the mountains of Southeastern Kentucky with a population of 5,381.[1] Due to the lack of any major highways and the absence of rail service, the county is somewhat isolated. The largest employer and the most important business in the county is the public school system. Entitlement programs, such as social security and food stamps, are the largest single sources of income for the county's inhabitants. The major industries and employers in the county are tobacco and coal mining. Logging is very active, but supplies only a few jobs because the trees, once cut, are shipped out of the area for further processing.

[1] Kentucky Population Research Center, University of Louisville, "1997 County Population Estimates."

COMMUNITY NEEDS

Along with making available quality account services and loan products, the Credit Union strives to provide financial education and money management to those with low incomes. Some observers argue that one of the major obstacles to development in this area is that welfare recipients have been discouraged from saving or owning their own cars or homes because of government imposed asset limits. These limits deny benefits to recipients who have combined assets and cash that exceed certain dollar amounts that are established by each state. However, recently enacted welfare reforms permit the states to increase those limits. Accordingly, on May 1, 1996, the Commonwealth of Kentucky allowed welfare recipients to save up to $5,000 in an IDA without losing their benefits.

BEST PRACTICE PROGRAM OR PRODUCT

In 1996, as a result of the Commonwealth's legislative reforms, the Credit Union entered into a partnership with the Mountain Association for Community Development ("Mountain Association") and the Owsley County Action Team (the "Action Team") to create an IDA investment instrument for low- and very low-income individuals and welfare recipients in Owsley County. The Owsley County IDA Program was developed to encourage people to invest in their future. IDAs are based upon the belief that poverty is best overcome through asset accumulation rather than income alone. The goal of the IDA program is to create a vehicle that enables individuals with incomes less than 125 percent of the Federal poverty level to set financial goals and invest their capital to attain those goals. According to Credit Union sources, the Federal poverty level currently established for a family of four in Kentucky is $20,045 in annual household income.

An IDA is an interest-earning savings account with restrictions placed upon use of the funds and the earnings on the account. The funds in an IDA accumulate much more quickly than a traditional savings account because the involvement of community organizations, financial institutions and state governments make it possible for additional monetary contributions to be made to the account. Use of IDA funds is restricted to those activities that have historically been connected to asset accumulation such as purchasing a home, starting a business or obtaining further education. While the accounts receive preferential tax treatment under applicable state law no preferential federal tax treatment for such accounts is currently available.

Nationwide, every IDA program is organized and managed differently. Here, the Action Team provided the initial outreach and served as the facilitator of core group planning sessions. These meetings were used to develop organizational structure, contractual agreements, policy guidelines and program objectives. All sectors of the community were allowed to contribute ideas and resources. Issues, such as term limits, monthly meetings, programs for additional learning, various types of available credit and post IDA initiatives, were addressed.

The role of the Action Team has changed as the program has evolved. The Action Team

IDA workshops and meetings, such as this meeting sponsored by The Action Team, are mandatory for all of the program's participants.

continues to provide community outreach and facilitate mandatory monthly meetings for program participants. The monthly meetings involve areas of development such as account maintenance, peer support an goal setting. The Action Team has recently added new services such as client screening, technical assistance, budget and credit counseling and home ownership education.

The Mountain Association wrote the initial grant proposals to fund the program's start-up costs. The Owsley County IDA program was awarded an initial $250,000 grant from the W. K. Kellogg Foundation, most of which was used to establish a Credit Union branch in Owsley County and to cover operational and administrative expenses. However, $37,500 was retained for matching the deposits of low- and very low-income IDA participants.

The Credit Union serves as the fiscal administrator for the IDA program. In this capacity, the Credit Union establishes savings accounts for participants, accepts deposits (most at the monthly meetings), and manages all IDA reporting mechanisms for the program. These mechanisms include monthly statements for participants, program audits and fiscal reports to partners and other funding sources.

Once an IDA participation agreement is signed, the IDA program participant opens two separate accounts with the Credit Union. The first account is the designated IDA account. The second is a regular savings account. The purpose of the second account is to establish the customer as a member of the Credit Union. Both accounts earn interest at the rate of 6.5 percent.

Each participant is expected to deposit $15 a month, or $360 over 24 months, in his or her IDA account. The IDA program contributes $6 for each $1 deposited, or $2,160 over 24 months, to increase the participant's incentive to save.

The Credit Union's IDA initiative is strictly a one-time only income assistance program. After individuals have achieved the 24-month investment goals, they cannot re-enter the program. Applicants may withdraw up to 10 percent from their IDA accounts, with no penalty, but the funds must be replenished within 30 days of withdrawal.

For those who wish to leave the program before completion of the 24-month cycle, their total contributions will be refunded, plus any interest accrued. However, all IDA matching funds, plus the interest on them will go back into the existing IDA pool. If a participant misses more than three of the mandatory monthly meetings, he or she will be automatically terminated from the program.

After the 24-month program is completed, all participant withdrawals must be cosigned by a representative of the Action Team. This ensures that the funds will be utilized for the agreed goals of the participant. Examples of some of the agreed upon goals are outlined below. If a participant decides to use the funds for a purpose that is different from the original goal, the participant must get approval from an Action Team representative. Additionally, if a participant decides not to use the funds at the end of the program, the funds will automatically default to an Individual Retirement Account.

EXPERIENCES AND OBSTACLES

The goal of the IDA program is to assist low-income individuals by providing them with $2,520 in savings plus interest to meet their needs in any of the following categories: (i) closing costs and down payment assistance on home purchases; (ii) home repair projects; (iii) higher education tuition and related costs; and (iv) micro-loan equity for small business development. For those interested in small business start-ups, the IDA program partnered with the Women's Initiative Network Groups for technical assistance and training. The Credit Union's President reported that most participants have been interested in saving for home rehabilitation projects.

The largest single problem in establishing an IDA program is getting it started. Generally, community outreach and education can be counted on to increase participation in the program, but these efforts take time.

CURRENT STATUS

Although most of the groundwork has been laid, the Owsley County IDA program is still in its infancy. Informational seminars for area residents began in April 1997. The first IDA account was opened in July 1997. Since then, the number of accounts opened has increased to 31. The combined participant contributions in those accounts total $2,508. The IDA program has matched those funds with an additional $15,047.

The program currently has the funding capacity to enroll 32 residents. If successful, this demonstration project could serve as a model for one form of welfare reform.

PARTNERSHIPS

The Owsley County IDA project is an initiative between the Credit Union, the Mountain Association for Community Economic Development, the Owsley County Action Team, Owsley County, community leaders, community residents, the Women's Initiative Networking Group, and the W.K. Kellogg Foundation.

Additional Information Contacts

Central Appalachia Peoples Federal Credit Union
Individual Development Accounts
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Berea, Kentucky 40403
Contact: Mr. Marcus Bordelon, President
Phone: (606) 986-8423
Fax: (606) 986-5836

Additional Resources

Kentucky State Data Center
Urban Studies Institute
University of Louisville
426 W Bloom Street
Louisville, Kentucky 40208-5457
Phone: (502) 852-7990
Fax: (502) 852-7386
Internet Home Page:
http://www.louisville.edu/cbpa/sdc

Kentucky Housing Corporation
1231 Louisville Road
Frankfort, Kentucky 40601-6191
Phone: 1 (800) 633-8896 (in-state only) or
(502) 564-7630
Internet Home Page:
http://www.kentuckyhousing.org/

TECHNICAL ASSISTANCE PARTNERSHIP

Florida Housing Coalition

PARTICIPANT PROFILES

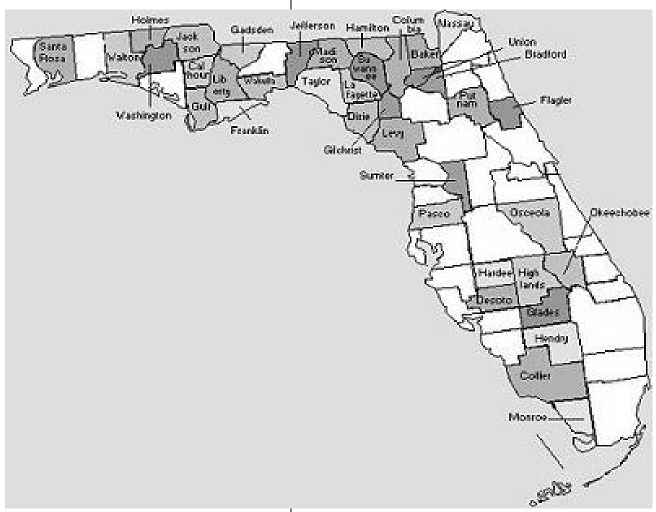
The Florida Housing Coalition, Inc., (the "Coalition") is a nonprofit statewide organization whose primary mission is to bring together housing advocates and resources. The Coalition provides training, technical assistance, and information on issues related to affordable housing. Through one-on-one training, telephone technical assistance, workshops and seminars the Coalition provides non-profit organizations with expertise in areas such as designing fiscal and program tracking systems, implementing regulatory reforms, compliance with state and federally funded housing program regulations and requirements, home rehabilitation and emergency repair programs, and developing volunteer programs. Further, the Coalition supports community-based partnerships in their efforts to maximize the availability and improve the quality of affordable housing in Florida.

The Coalition is Florida's largest public/ private housing partnership. Since its incorporation in 1982 as the Rural Housing Coalition, membership has expanded from a handful of organizations and individuals in the Orlando area to almost 400 groups and individual members located throughout the state. In the organization's early years, one-on-one assistance to Florida's rural communities was the highest priority. Assistance to Florida's rural communities was particularly needed as housing professionals in those areas were often isolated and had more limited access to resources than their urban counterparts. Today, this well-organized network allows the Coalition to bring a unique strength and wealth of experience to the task of providing training and technical assistance to all of Florida's local governments and community-based organizations.

The Coalition's technical assistance team includes individuals from its highly skilled staff, current practitioners, and housing professionals in virtually all areas of affordable housing development. The Coalition, headquartered in Tallahassee, operates with a staff of nine employees located in five offices throughout the state, including one located in the rural community of Inverness. Additionally, approximately 20 experienced housing professionals, who voluntarily serve on the Coalition's Board of Directors, act as members of the technical assistance team. They provide on-site and telephone consultation and serve as presenters and instructors for workshops and conferences.

COMMUNITY BACKGROUND

Florida is a peninsula state stretching 850 miles from its northwest boundary near Pensacola to its southernmost tip in Key West. The state spans 58,560 square miles. Florida is the nation's fourth most populated state, and has a rural population of 2.2 million people. Although less than 20 percent of the state's population live in rural communities, more than 80 percent of the state's land and natural resources are considered rural.[1]



Rural Florida, which includes 37 counties, is geographically and economically diverse. Farming communities are located primarily in the Panhandle and southern Florida counties. Manufacturing communities have given way to tourism in the central region around Orlando. The rural counties with the highest unemployment rates are all in the highly agricultural areas of Central and South Florida.

Tourism is the state's leading industry, attracting over 40 million people annually, including millions to rural Florida attractions such as the Everglades. The state's mild climate, extensive coastlines and lakes have attracted thousands of retirees. These characteristics of rural Florida have presented a myriad of problems in terms of managing growth. While the settlement and development of many rural areas has brought employment, primarily in the service sector, most of the jobs pay low-wages.

The decline of resource-based industries has been felt throughout rural Florida. For example, the state, in an effort to improve water quality and other environmental conditions, has purchased farmland and converted thousands of acres to conservation uses. These efforts have further distressed the economies of the rural communities by changing the economic base and increasing unemployment.

[1] Executive Office of the Governor of Florida, "A Blueprint for Rural Florida," (January 1998).

COMMUNITY NEEDS

Retirees and tourism are staples of the state's economic growth, but their presence has escalated the price of housing, particularly in rural communities. Those areas that were once considered too remote for development have become prime targets for individuals desiring to purchase land and build homes in unspoiled natural settings. This influx of new residents has not only increased the price of homes, it has created a shortage of available land for building affordable housing.

These developments have, in turn, put additional burdens on agencies and organizations attempting to assist low- and moderate-income individuals in these areas. For rural government agencies and community-based organizations receiving funding to enhance housing development activities, the need for strong reporting and effective administration skills is essential to perpetuating long-term quality programs. The Coalition provides them with training and technical assistance to accomplish these goals.

BEST PRACTICE PROGRAM OR PRODUCT

The work of the Coalition in the 1980s focused heavily on disseminating information, utilizing print news networks, and statewide conferences. Its work in rural communities was targeted at bringing together community-based organizations, lenders, civic leaders, utility companies, civic groups, church organizations and other advocates to develop affordable housing plans.

In 1991, aware of the importance of having a dedicated source of revenue for affordable housing in the state, the Coalition's members were active proponents of an intense statewide effort to pass the William E. Sadowski Affordable Housing Act ("Sadowski Act"). The Sadowski Act, which became law in 1992, established a badly needed trust fund for affordable housing initiatives, particularly in Florida's rural communities. A portion of the funds supported state-sponsored housing development programs administered by the Florida Housing Finance Corporation.

The Sadowski Act also led to the creation of the State Housing Initiatives Partnership ("Housing Initiatives Program"). Through the Housing Initiatives Program, administrators in local governments received direct appropriated funding to create or facilitate housing development activities. Housing Initiatives Program funds have been used to develop a number of innovative programs throughout the state. For instance, in 1997, Lee County used $45,000 of its Housing Initiatives Program funding to leverage the development of an 81-unit rental facility, Pearl Harbor Apartments, for very low-income and special needs renters. Additionally, the county allocated $5,000 to conduct a farm worker housing needs study in the area.

Until the Sadowski Act, for which appropriations were initially made in 1992, financing for housing initiatives was limited and administered by consultants, local government officials, or community-based organizations. However, this new level of state funding required that training and technical assistance be available to help administrators increase their capacity to develop meaningful housing strategies and to leverage available funds with private sources. This led to the creation of the State Housing Initiatives Partnership Catalyst Program ("Housing Catalyst Program").

The Housing Initiatives Program funds enabled many smaller cities and counties to administer local affordable housing programs for the first time. The Housing Catalyst Program, which was also funded through the Sadowski Act, made available technical assistance for administrators receiving Housing Initiatives Program and State HOME [Home Investment Partnerships Program] dollars. Having access to training and technical assistance from experienced, qualified professionals was vital to administrators in rural communities.

In 1993, through a contract with the Florida Department of Community Affairs, the Coalition was designated as a Housing Catalyst Program technical assistance provider. For the Coalition, the Housing Initiatives Program funding meant that the work the staff, board members, and volunteers had performed since 1985 would be continued and expanded throughout the state.

Technical assistance workshops , similar to one provided by FHC in Calhoun County, FL are important to assimilating new information to rural communities.

Initially, the Coalition’s technical assistance team provided training and technical assistance in the form of workshops and telephone consultation. Recognizing that workshops and theory were not enough, the Coalition's technical assistance team crossed the state for nine months, making 43 on-site visits to 28 counties during the first year of the Housing Catalyst Program. Each Coalition site-visit was tailored to meet the specific needs and objectives of the Housing Initiatives Program administrators.

The Coalition continued to provide direct training and technical assistance under the Housing Catalyst Program to the Housing Initiatives Program, state HOME and other affordable housing programs. In 1997, the Coalition conducted 103 on-site visits and answered 325 requests for telephone technical assistance. Additionally, the Coalition conducted three Regulatory Reform workshops, in November and December, which attracted more than 145 Housing Initiatives Program administrators. In 1998 this work was expanded to include a contract for 16 technical assistance workshops throughout the state.

The Coalition’s technical assistance expertise is not limited to the Sadowski Act initiatives. As The Enterprise Foundation's Florida-based partner, the Coalition provides Community Housing Development Organizations with intensive technical assistance. The training includes organizational management, leveraging of funds, program design and administration, and other operational issues. During 1996-97, the Coalition worked with 15 Community Housing Development Organizations.

The Coalition does not just provide training and technical assistance in the area of low-income housing. The non-profit is a partner in the Florida Community Development Initiative, which was formed in 1996. This joint effort between the Coalition and the Florida Community Loan Fund provides low-interest loans and free technical assistance to community-based organizations that specialize in working to improve housing and economic conditions in their communities. The Florida Community Loan Fund provides capital to qualifying organizations, and the Coalition provides borrowers (and potential borrowers) with the technical assistance needed to complete their affordable housing and economic development projects.

In addition to its training and technical assistance efforts, the Coalition remains consistently in the forefront in disseminating affordable housing and training information. It publishes quarterly a technical journal called the Housing News Network that focuses on current housing, training, and legislative issues. The Coalition also maintains a home page containing housing-related information that is updated on a weekly basis. The Coalition's most successful outreach initiative is an annual statewide affordable housing conference, which is designed to focus on current issues and partnership-building initiatives. Sponsored each year by the First Union Foundation, SunTrust Banks of Florida, the Florida Department of Community Affairs, and the Florida Housing Finance Corporation, the conference draws government officials, non-profit organizations, financial institutions, builders, realtors, and social service agencies. In 1997, the conference's tenth anniversary, the event attracted more than 300 participnts.

To fund its 1997 programs, the Coalition received 63 percent of its $400,000 in revenues from training and technical assistance contracts. Contributions included 14 percent from private foundations, 12 percent from Partners for Better Housing memberships, and 11 percent from Annual Conference income and memberships.

Experiences and Obstacles

Although the Coalition has been very successful in advocating housing technical assistance and training, there has been a marginal relationship between the non-profit and the banking community. Programs like the Coalition are working to educate financial institutions on the benefits of technical assistance to all aspects of affordable housing. This assistance improves the performance of both local housing non-profit organizations and their lenders and partners.

The Coalition emphasizes the importance of lender partnerships, as well as partnership building, as a necessity to its continued success. As part of its partnership development strategy, the Coalition has made a conscious effort to include financial institutions on its Board of Directors. This is important because all members of the Coalition's Board of Directors actually provide training and technical assistance to Coalition clients. For example, the Coalition currently has a representative from NationsBank and one from First Union who serve as trainers and presenters at conferences and workshops.

Lender sponsorship of the Coalition's technical assistance and training initiatives has become a key focus of the organization's fundraising strategy. Through a program called "Partners for Better Housing" the Coalition solicits sponsorship for its ongoing technical assistance and partnership development work. Of the Coalition's 37 partners for this program 12 are financial institutions.

CURRENT STATUS

In a project with the Florida Developmental Disabilities Council, the Coalition was contracted to increase rental and home ownership opportunities for persons with developmental disabilities. In 1997, its second year of the two-year contract, the Coalition provided technical assistance through on-site visits and consultation to more than 100 social service providers. Additionally, the project has developed four housing demonstration programs throughout the state by leveraging $2 million.

In 1998, in a project with the Florida Department of Community Affairs, the Coalition is focused on the integration of energy efficiency into affordable housing programs. The Coalition's technical assistance team will inventory what energy measures are currently included in housing programs, investigate what energy initiatives are available in the state, and recommend methods for better linking these housing and energy programs.

The goal of the Coalition is to ensure that energy efficiency is incorporated into every housing unit receiving public funds in the state. The Coalition hopes to meet this objective by providing training on energy efficient housing rehabilitation and integrating energy conservation programs into local housing partnerships.

In 1998, through a contract with the Housing Assistance Council, the Coalition is providing specific organizational capacity technical assistance to a rural housing organization called the Partnership in Housing. The goal of the training is to enable the organization to obtain funds to build an 80-unit farm worker housing community. The Coalition's technical assistance included strategic planning, budgeting and operation management.

PARTNERSHIPS

The Coalition's broad-based membership includes city, county and state governments, private non-profit and for profit organizations, individuals, financial institutions, local housing groups, real estate professionals, builders, housing authorities, homeless coalitions, housing counselors, attorneys, church groups, social service providers, state associations, advocacy groups and utility companies. The Coalition also serves as the Florida link for several national organizations such as the National Low Income Housing Coalition, the Center for Community Change and the National Congress of Neighborhood Women.

ADDITIONAL INFORMATION CONTACTS

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SMALL BUSINESS DEVELOPMENT EQUITY INVESTMENT

First Citizens National Bank

PARTICIPANT PROFILES

First Citizens National Bank ("First Citizens" or the “Bank”), a wholly owned subsidiary of First Citizens Financial Corporation, is a federally-chartered commercial bank in Mason City, Iowa, located in Cerro Gordo County, has assets of approximately $530 million, 11 branches and operates in 8 counties, including rural Floyd County. First Citizens is recognized as a financial services leader for commercial and agricultural businesses in North Central Iowa. The Bank has committed financial and staff resources to the ongoing growth of loan and deposit services to meet the needs of this important market segment.

COMMUNITY BACKGROUND

According to the 1990 Census, Iowa's total population at that time was 2.7 million. The Census Services Department of Iowa State University (“ISU”) estimates Iowa’s total population as of July 1, 1996, to be 2.8 million. Floyd County is a small community located in North Central Iowa. According to 1990 Census data, Floyd County had a total population of 17,058. Notwithstanding the increase in total population for the state, ISU estimates that Floyd County’s total population dropped to 16,538 as of July 1, 1996. Historically, this county’s economic strength has been its farming and manufacturing industries. Farming-related businesses have been steadily declining since the agricultural crisis of the 1980s. However, the manufacturing and processing industries

remain a significant and vital part of the local economy. According to the Iowa Department of Economic Development, the total non-agricultural labor force as of 1996 was 7,686, or 87.8 percent of Floyd County's entire labor force. The U.S. Census Bureau estimates that the 1993 average median income for the county was $27,607. According to the Department of Economic Development, the unemployment rate for June 1998 was 3 percent.

The county seat of Floyd County is Charles City, a community with 8,000 residents and a relatively low cost of living. The city's climate is ideal for manufacturing and service industry development. The major employers in the county include Fort Dodge Animal Health, Salsbury Chemicals, All-State Quality Foods and the Floyd County Memorial Hospital.

COMMUNITY NEEDS

Floyd County has been adversely affected by the loss of a major manufacturing employer. The company, which manufactured farm tractors, laid off nearly 1,500 people during its last 10 years in business and only 408 employees were on the payroll when the plant permanently closed in 1993. The plant's closing left an enormous employment gap in the local community. Without a growing industry or new employer to supplement the loss of the manufacturing plant, the creation of a diversified employment base seemed the best option available for pulling the local economy out of its slump.

BEST PRACTICE PROGRAM OR PRODUCT

In 1994, local government and business leaders held a series of meetings to address employment issues and devise a strategy for long-term economic recovery. A key resource in the planning was a 1991 economic case study conducted by the University of Northern Iowa's Community Economic Development Program. The study concluded that rural communities, once dependent on sector industries[1] or large employers, found new opportunities by diversifying their economic bases and attracting small businesses, i.e., those with 20 to 100 employees. The study also noted that these communities were more successful at getting new businesses to locate in their towns when there was a suitable industrial building available for purchase or rental.

One of the major initiatives resulting from the deliberations was the creation of the Floyd County Progressive Growth Limited Liability Company ("LLC"). The mission of this multi-investor, for-profit organization was to maximize the use of the combined resources of its members to attract small businesses and create employment opportunities for low- and moderate-income people in Charles City and Floyd County.

In order to participate in the LLC, First Citizens had to obtain the approval of its primary regulator, the Office of the Comptroller of the Currency ("OCC"). The OCC approved First Citizens' equity investment in the LLC pursuant to 12 U.S.C.A. § 24 (Eleventh) (1997) and 12

C.F.R. Part 24 (1997). Part 24 specifically authorizes national banks to make investments designed primarily to promote the public welfare.

In 1995, the LLC began laying the foundation to oversee and administer this economic growth initiative. The LLC's sole purpose was to provide the Charles City Area Development Corporation ("City Development") with an industrial building as part of the expansion of an existing industrial park and with the resources necessary to provide an incentive for prospective employers to locate in the community. However, in the early stages of development the LLC had no staff or operating budget. As a member of the LLC, City Development agreed to make in-kind contributions of administration, marketing, sales, and staff support for the LLC. These contributions helped make it possible for the LLC to fulfill its mission.


Above is the 50,000 sq. ft. industrial spec building, located in Charles City, IA. The facility has attracted more than 100 inquiries from small businesses.

The LLC planned to expand the development of an existing industrial park complex on the southwest side of Charles City. An integral component of the plan was a proposed 50,000-square-foot building that could be purchased or leased by small industries for manufacturing or other enterprises.

The industrial building, which was the only major asset of the LLC, had projected construction costs of $500,000, and was on a five-acre parcel of land. Its construction was very basic, with many unfinished features. The idea behind this approach was to keep the cost down and give new companies the flexibility to develop the site to their own specifications. This, in turn, was projected to stimulate community job growth.

Initially, six members, including First Citizens, each invested $125,000 in the LLC, enabling it to purchase and develop the industrial building. Under the terms of the partnership, the initial investment capital, which was non interest bearing, could not be recovered until the building was sold.

The land, then valued at $40,000, was transferred to the LLC by a private landowner, and a local contractor agreed to develop the land and construct the industrial building at wholesale cost. Both the landowner and developer agreed to defer their compensation until the property was either sold or it was 75 percent occupied by tenants. The cooperation of the landowner and the developer, as well as capital contributions of the LLC members, were critical to the success of this venture because they enabled the LLC to construct the facility without incurring any debt.

In addition to the development of the building, various community entities developed creative strategies for attracting new business activity to Charles City. For example, Charles City and Floyd County created the Tax Incremental Financing District ("TIF District"). The objective of the TIF District was to provide front-end financing to be repaid from future tax assessments. With the TIF District incentive, new businesses could receive tax-financing payable over 7-10 years. This joint initiative represented one of the first city/ county TIF District ventures in the state of Iowa.

Another tax incentive for new businesses in Charles City was made available by the Enterprise Zone legislation. The incentive became a reality under an Iowa State law, passed in 1997, that created Enterprise Zones for designated communities; both Charles City and Floyd County received this designation. The Enterprise Zone legislation allowed Charles City to provide tax abatements, which would also be used to attract new businesses to the city. In awarding a business up to 10 years of property tax abatement, the city and county are confident they are attracting a business that will be providing economic benefit to the community long after the term of the abatement has expired.

With the administration, funding and tax incentives in place, the next step for the LLC was to utilize the partnership's resources to effectively market the industrial building and complex. The marketing strategy focused on the industrial building, the TIF District, and the Enterprise Zone to attract small businesses into the area. As part of the marketing strategy, photographs of the building were placed on the Internet and featured in brochures distributed by the Iowa Department of Economic Development and the Mid-American Energy Company, an LLC equity member. Additionally, advertising campaigns produced by various city, county, and state government agencies featured the industrial park and building.

As a partner in the city's economic development initiatives, First Citizens also made a $100,000 contribution to a newly created Job Incentive Capital Fund. The $500,000, which was privately and locally raised by City Development, provides "start-up" subsidies for small businesses relocating to the area. The cash incentives can be in the form of interest buy-downs, a lease subsidy, or a forgivable loan or grant for other purposes. It gives small employers an added incentive to create jobs and opportunities in the community.

[1] Examples might include manufacturing, textiles, crop farming, livestock farming, and tourism.

EXPERIENCES AND OBSTACLES

The experience of the LLC over its three year history has been that of cooperation and collaboration among the members, City Development, the community, the county and Charles City. The long term goal of creating jobs and economic health for the County has remained the central focus of the organization. Enterprise Zone designation and the establishment of the joint city/county TIF District were accomplished in a timely manner through the cooperative efforts of all parties.

Obstacles to the success of selling or occupying the building include the highly competitive nature of economic development. Similar incentives are available in other communities of varying size throughout Iowa and the Midwest. The LLC members entered into the project with the full knowledge that economic development is a long term goal, requiring patience and determination.

CURRENT STATUS

Since the LLC opened its doors for business in 1995, there has been increased interest in Charles City. In 1997, the industrial building attracted more than 100 inquires from small businesses interested in purchasing or leasing the property. To date, 12 of those proposals have developed into solid prospective industrial candidates. One prospect in particular considered the industrial building for a start-up manufacturing business, but selected another building in Floyd County. Clearly, the industrial building and the above-identified financial incentives were the reasons that the company was initially attracted to Floyd County. The economic impact of the company will be 20 jobs over the next two years at an average wage of $13.50 per hour.

The LLC is very close to finalizing an agreement with Winnebago Industries to lease the industrial building for the purpose of establishing a satellite facility in Charles City. Winnebago plans to utilize the site to produce components for shipment to the parent facility. Successful negotiations would result in a minimum of 100 new jobs to Floyd County with hourly wages ranging from $8.05 to $27.50. At least 51 percent of the positions created would be taken by or made available to individuals from low- and moderate-income households. Charles City is being considered as a manufacturing location by Winnebago in part because of the available work force, the industrial building and the financial incentives available through the Enterprise Zone qualification, the local Jobs Incentive Capital Fund (projected at $300,000 or $3,000 per job), the Iowa Department of Economic Development Set-Aside Program (projected at $300,000), and the City/County TIF District grant (projected at $350,000). The estimated cost f developing the manufacturing site is $1.9 million. The economic development incentive package being offered would enable the company to significantly offset those costs. The success of this pending project will be a significant validation of the value of partnerships between private and public entities in fostering economic development in rural communities.

The LLC's economic development operations have expanded geographically. In 1998, a non-profit organization called the Northern Prairie Regional Economic Development Corporation ("Northern Prairie") was created to foster economic development activities throughout Floyd County. Charles City and Floyd County put up $30,000 each as venture capital to further develop the Northern Prairie initiative. The participation of the non-profit will enable small business support initiatives to reach outlying regional communities. The addition of a non-profit entity can be another important tool for attracting resources for economic development. Many philanthropic organizations are only able to fund non-profit initiatives.

PARTNERSHIPS

The comprehensive economic development initiatives of the LLC were made possible with the cooperation of the following entities: First Citizens National Bank, the State of Iowa Department of Economic Development, the Charles City Area Development Corporation, the University of Northern Iowa, the City of Charles, Floyd County, First Security Bank & Trust, Mid-America Energy Corporation, Point Builders, Northern Prairie Regional Economic Development Corporation, and the Charles City Civic Foundation.

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http://129.186.33.245/census/

Division of Community & Rural Development
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http://www.state.ia.us/government/ided/crd/index.html

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PARTICIPANT PROFILES

Community Equity Investments, Inc. ("Equity Investments") is a Community Development Corporation ("CDC") that was incorporated in 1974 as a federally funded CDC. A grant from the Office of Economic Opportunity, part of the "War on Poverty" initiative by the Johnson Administration, provided Equity Investments' initial funding. Equity Investments is a community-controlled, non-profit organization. The Board of Directors is composed of 21 members, 11 of whom are elected by the residents of Escambia County, Florida.[1] Equity Investments operates on an annual budget of $800,000 and has a 13-member salaried staff that includes a Vice President of Lending Operations, two Loan Officers and a Technical Assistance Specialist.

One of Equity Investments' principal products and the subject of this best practice review is its microlending program, undertaken with the help of a program sponsored by the Small Business Administration ("SBA"). Discussed in greater detail below, microlending is generally defined as the making of small business loans under $25,000 to help stimulate the creation of jobs and promote business ownership opportunities for low-income borrowers. Equity Investments operates a very successful Revolving Loan Fund, established with funding from the Florida Department of Community Affairs, an Intermediary Re-lending Program (USDA Rural Development), and an affordable Home Ownership and Housing Rental Program. Equity Investments spearheaded a 1992 initiative to enhance minority business opportunities in the region through the development and support of the Northwest Florida Black Business Investment Corporation.

Funding is derived primarily from earnings generated by its programs, including the Revolving Loan Fund outlined above and the Micro Enterprise Loan Program described below, rental income and the sale of single family units. A small annual grant is received from the Florida Department of Community Affairs for general administration. A larger annual grant is received from the SBA for training and technical assistance services to the SBA's Micro Enterprise Loan Program ("Microloan Program").[2]

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[1] Horvath, R. Daniel. "Partners in Community and Economic Development: CEII." Federal Reserve Bank of Atlanta. 1997. P. 6.
[2] Ibid.

COMMUNITY BACKGROUND

Over the years, Equity Investments has grown from a neighborhood based CDC in Escambia County to a regional CDC. Currently, Equity Investments has a lending territory that covers the 15 county area of the Florida Panhandle. Bordered by Alabama in the northwest and the Gulf of Mexico in the south, the area includes a mixture of urban and rural communities. The area's largest urban centers are Pensacola, Tallahassee, and Panama City. The 1990 Census indicates that the population of the region at that time was 992,903. As of July 1, 1997, the U.S. Census Bureau estimates that the population of this area had increased to 1,155,993. In 1989, per capita income for the 15 county region was $10,828. This amount rose to $13,157 in 1993 and, as of 1997, is estimated to be $17,264.

The majority of the region's housing stock consists of single family detached units. According to the 1990 Census data, eighteen percent of the 106,174 county households were single-parent families and more than one-forth had incomes below $24,999. The primary area of housing growth is in the new construction sector where homes are moderately priced between $60,000 and $80,000. Only minimal building activity has taken place in the $25,000 to $50,000 price range.

The region is largely dependent upon employment opportunities in tourism, retail and the government sectors. For example, the Pensacola Naval Air Station is heavily dependent on a civilian workforce, but the federal government's closing of the Naval Aviation Depot in Pensacola has resulted in the elimination of 3,500 technical civilian jobs and the loss of almost $150 million annually to the local economy. Efforts to attract new businesses to the area or to encourage existing businesses to expand their operations in the region have met with some success and have helped offset some of the loss of jobs that occurred as a result of the Naval Aviation Depot closing.

COMMUNITY NEEDS

Equity Investments' microloan program is aimed at creating small business growth and new job opportunities for residents of its lending territory. The term "microloan" refers to business loans with principal amounts between $500 and $25,000. SBA sponsored microlending programs are only available to non-profit organizations and are used as a vehicle to stimulate low-income entrepreneurial business opportunities by providing specialized funding for these businesses. For example, Equity Investments' borrowers have opened day care centers, hair salons, restaurants, and travel agencies. Many state governments have implemented strategies to ensure that microloans and small business lending are tied to economic growth. For example, Florida has enacted legislation to tie job creation to state-funded initiatives. Therefore, Equity Investments carefully tracks job creation in order to make sure it complies with the Florida statutory requirement that at least one new job be created for every $10,000 in loans.[3]

In rural communities, microlenders fill a void because of the lack of conventional lenders willing and able to make these small loans. Some small rural areas have only one or two lenders that service their community. Additionally, banks with branches in rural communities often do not have the products, expertise, or service capacity needed to address the microloan borrower. Furthermore, rural communities are generally perceived to lack the population density needed to support the start-up or expansion of microloan businesses. This factor has caused conventional lenders to view the microloan business as an extremely risky venture.

Historically, small business loans under $25,000 have not been profitable for banks because of the originating, processing and servicing costs associated with such loans. The small size of microloans means that bank fees, typically based upon a percentage of the loan amount, do not provide sufficient profit to justify making these loans. Additionally, many microloan applicants need considerable training and technical assistance. These ancillary costs further reduce the attractiveness of such programs to traditional financial institutions.

As a microlender, the operating objective of Equity Investments is to develop this crucial niche market with the overall social goal of providing financing, technical assistance and opportunities to unserved and under served customers. Through microlending initiatives such as that undertaken by Equity Investments, low-income borrowers obtain financing that enables them to start up their businesses, gain experience, and establish a demonstrable track record. For successful microloan businesses, this translates into larger loans for conventional lenders in the future.

[3] Ibid. P. 7.

BEST PRACTICE PROGRAM OR PRODUCT

Equity Investments became one of the first 35 intermediaries selected to participate in a new SBA Micro Enterprise pilot program to provide small business loans of under $25,000. Equity Investments established its Microloan Program to stimulate job creation and promote business ownership opportunities to low-income borrowers in the Florida Panhandle. To this end, Equity Investments' Microloan Program sought to provide technical assistance and business training to help low-income borrowers establish and maintain self-sustaining businesses.

Under the agreement executed with the SBA, Equity Investments received an initial $500,000 loan to provide microloan financing. The SBA loan is for 10 years at 5 percent interest. Equity Investments has closed two additional SBA loans totaling $1.5 million. A fourth loan for $500,000 has been approved and will be used by Equity Investments to begin making microloans in the Southern Alabama market. These funds are utilized by Equity Investments to fund microloans to individual borrowers. The individual microloans are not guaranteed by the SBA.

Equity Investments also receives an annual SBA grant, the amount of which is usually set at 20 percent of the cumulative loan balance due to the SBA. The grant covers program marketing up-front technical assistance such as business strategy development market analysis, and post loan counseling. Another condition of the Microloan Program is that all applicants must reside in Equity Investments' designated service area.

Equity Investments conducts an extensive marketing effort to reach potential borrowers. Equity Investments advertises the Microloan Program through the local municipalities, non-profit organizations, radio stations and newspapers. However, 80 percent of the referrals to Equity Investments come from the area's financial institutions. Often local banks cannot make these type of loans profitably, but they want to keep their existing customers. Having an organization like Equity Investments available to refer customers to is beneficial for the banks. Equity Investments' President has indicated his belief that because of the specialized nature of the Microloan Program, a bank's referral of its customer to Equity Investments does not result in a lost customer. Further, he believes that helping customers find specialized credit that is not available from the bank likely improves the customer's relationship with the bank. Finally, the Microloan Program serves as an entrepreneurial incubator for unproved small businesses that may develop into future customers for conventional lenders.

Equity Investments provides potential applicants with a package that describes the program and contains a loan application form, credit release form and other materials relevant to the program and application process. If necessary, Equity Investments also supplies technical assistance to applicants seeking help in completing their application or assembling necessary documentation. Equity Investments loan officers pre-screen potential borrowers for compliance with product requirements and to ensure that the applicant resides in Equity Investments' service area.

Once the application is complete, the loan officer packages, underwrites and prepares the loan for the Loan Review Committee (the "Committee"). The Committee consists of representatives from financial institutions, private industry, and community residents. The borrower's capital, collateral, capacity, and credit are evaluated by the Committee, which then makes its recommendations to the Board of Directors. The Committee and the full Equity Investments Board of Directors must approve all loans. If a loan is denied, Equity Investments has an appeal process that affords the applicant himself or herself the opportunity to present the loan to the Board of Directors.

The Committee generally sets the loan terms and conditions, particularly with regard to

Pictured is Doug's Bar BQ which was financed with a $25,000 micro-loan from CEII. The restaurant, which opened its doors for business in 1994, is located in Santa Rose County, FL

collateral requirements. For example, one Equity Investments microloan and extensive technical assistance enabled a disabled veteran to establish a dine-in restaurant and catering business in Milton, FL. The entire project required $90,000 in financing. Equity Investments was able to loan the borrower $25,000 based on his overall application, credit history and collateral. One strong consideration in making this loan was the fact that the borrower was able to pool together other resources, including $30, 000 from his personal savings, to come up the remaining funds. The terms of this microloan were 5 years at 8 percent interest. Generally, microloans are made for up to five years at 8 to 12 percent interest. However, the smaller loans, those between $5,000 and $10,000, typically have repayment terms of 2 or 3 years, depending on the borrower's financial capacity. Loan approval normally takes about four weeks.

All approved loans are closed in-house by Equity Investments and there are no closing fees. If a loan contains a real estate component, an Equity Investments approved attorney or title company closes it. The SBA does not permit the sale of microloans, therefore, microloan lenders are required to handle all loan servicing in-house. This requirement forced Equity Investments to develop an in-house loan servicing capacity.

Currently, the success rate on all outstanding Equity Investments microloans is about 93 percent. A number of factors combine to keep the default rate so low. The 20% grant provided by the SBA described above offsets the considerable cost incurred in providing up-front training, technical assistance and post loan counseling for microloan borrowers. Most Equity Investments applicants have limited expertise in business financing and operational management. Thus, the level of one-on-one technical assistance provided to a typical borrower by Equity Investments loan officers, both before and after the loan is closed, far exceeds the technical assistance provided by a conventional bank loan officer to one of their clients. Further, 50 percent of the technical assistance provided by Equity Investments is done after the loan is closed. Providing all of these perpetual services contributes to the Microloan Program's minimal loan defaults.

EXPERIENCES AND OBSTACLES

Non-profit organizations such as Equity Investments may be the only entities capable of making significant numbers of microloans. As discussed briefly above, traditionally, conventional financial institutions have not shown a significant interest in providing microloans because of their high maintenance cost and the small loan balances that many believe make them unprofitable. The small size of microloans means that bank fees based on a percentage of the loan amount simply don't provide sufficient profit to justify offering these type of loans. For example, a $25,000 loan with a 2 percent origination fee would only yield $500. Finally, microloan borrowers typically have a limited amount of collateral available, which makes these loans riskier.

However, the new Community Reinvestment Act ("CRA") regulations have placed a greater emphasis on lender investments that encourage community economic development. Through the new CRA regulations federally insured depository institutions are able to receive full CRA credit for microloan investments if the loan is made to a Community Development Financial Institution (CDFI) and the lender is a participant in the Bank Enterprise Award (BEA) Program.

The emerging market for microloans has created potential partnerships for Equity Investments with conventional lenders like banks and thrifts. In 1997, Equity Investments received grants from the following banks: First Union National Bank ($7,500), SunTrust Bank ($5,000), Chase Manhattan Bank ($5,000), and Compass Bank ($2,500). In 1998, SunTrust also authorized a $50,000 low-interest loan for Equity Investments to use in funding microloans. Further, these financial institution loans and grants to microlenders like Equity Investments are given strong consideration by regulators when evaluating financial institution performance under the CRA lending and investment tests.

CURRENT STATUS

Equity Investments made its first micro enterprise loans in 1992. Since then the Microloan Program has grown to its present loan portfolio level of 105 loans totaling $1.6 million. The Microloan Program's lending profile includes 41 percent start-up companies and 59 percent expansion of existing businesses. Further, 40 percent of the borrowers are minorities and 35 percent are women. The average loan size is approximately $16,000 and through its Microloan Program Equity Investments has created or maintained a total of 210 jobs.

After six years of dispersing microloans to Northwest Floridians, Equity Investments was ready to expand the product into Alabama. In November 1997, Equity Investments received permission from the SBA to make the product available to a 13-county area in southern Alabama.

PARTNERSHIPS

Equity Investments is able to engage in microlending because of the program implemented by the SBA. In addition, Equity Investments obtains strong support from the region's financial institutions, local and state governments and the citizens of the area.

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AGRICULTURAL LENDING

First National Bank of Shelby

PARTICIPANT PROFILES

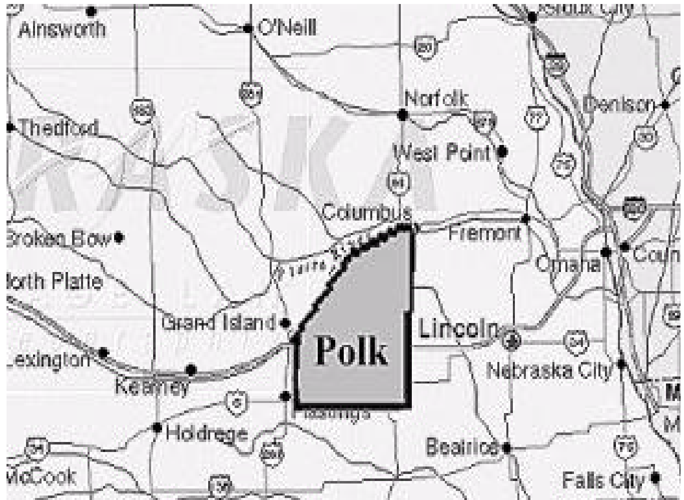
The First National Bank of Shelby ("FNB-Shelby" or “the Bank”) is located in Shelby, Nebraska and has approximately $23 million in total assets. FNB-Shelby is a subsidiary of Pinnacle Bancorp, Inc., a bank holding company created in 1993 that owns 19 banks located throughout Nebraska, Colorado, Wyoming and Kansas, and has total assets of $1.9 billion.

FNB-Shelby has become a significant agricultural lender in the central Nebraska region and also has become very aggressive as a residential mortgage lender. The Bank, which had only $42,000 in residential mortgages in 1992, added an array of competitive mortgage products and programs and had, by year end 1997, increased its volume more than 70 times over its 1992 level, including FHA and VA loan originations. The Bank also is a very active lender in federally guaranteed loan programs, such as the Farm Service Agency[1] and the Small Business Administration (“SBA”). Moreover, FNB-Shelby has established a diverse portfolio of consumer and community development loans, as well as having become more active in long-term, fixed rate agricultural real estate and acreage lending.

[1] The Farm Service Agency was formed during the Department of Agriculture’s 1994 reorganization. It incorporates programs from several agencies, including the Agricultural Stabilization and Conservation Service, established by Congress in 1935 to give committees of local farmers a voice in how Federal programs are implemented in their counties. Programs from the Farmers Home Administration and the Federal Crop Insurance Corporation also were incorporated into the Farm Service Agency.

COMMUNITY BACKGROUND

FNB-Shelby's primary lending market is Polk County, located 83 miles west of Omaha, Nebraska. The U.S. Census Bureau estimates that Polk County’s population as of 1997 was 5,628. Employment in Polk County is primarily concentrated in the agriculture industry and a growing services industry. The 1990 census revealed that the county had a total labor force of 2,583 workers, with farm-related employment accounting for 710 of these jobs. The largest non-farming employer is the local government, which, in 1990, employed 511. According to 1998 data from the U.S. Department of Housing and Urban Development, estimated median family income in Polk County is expected to be $41,800. The Bureau of Business Research for the University of Nebraska-Lincoln estimates that the county's unemployment rate was 2 percent in 1995 and, as of April 1998, it may be as low as 1.6 percent.



Shelby, a town estimated in 1996 to have just 680 inhabitants – 10 fewer than the 1990 census – is located on the eastern edge of Polk County. The primary economic activities in Shelby are farming, cattle feeding, hog production, and retailing. There is very little manufacturing activity, but the service industry continues to grow. Since 1995, eight businesses have built or purchased and renovated buildings in the town. Public/ private businesses, such as the FNB-Shelby, the Post Office, a senior/community center, and a public library, have enhanced the community and stimulated economic development.

Further economic development progress can be seen in the housing sector. Nine new homes were constructed during the past two years at an average cost of $125,000. This was in stark contrast to the average cost of existing single family homes, which was only $29,000. Of the new homes constructed, seven were single-family and two were duplexes. The town also has one low-income multi-family dwelling.

COMMUNITY NEEDS

In Shelby, agriculture is an integral part of every day life. Whether it is crops or livestock, agriculture-related businesses are essential to the area economy. The agriculture industry, however, is facing political and economic changes that are making local lending more complex and competitive. The 1996 Farm Bill imposed limits on federal spending beginning in 1996. While there was a slight increase in spending in 1996 and 1997, federal funding will decrease from $5.8 billion in 1998 to $4.008 billion in 2002.[2] Federal farm subsidies, which are being reduced, provide both the farmers and the lenders with some sense of security. When land is farmed under price supports from the federal government, the farmer has a guaranteed market and a guaranteed price for a least a percentage of his crop. Without the price supports, lending becomes more difficult. An element of risk is added to a business that is already burdened with more potential pitfalls than most.

In addition to the uncertainties presented by reduced federal funding for farmers, banks and thrifts are finding that a greater share of the farm market is being handled by nontraditional lenders such as insurance companies and mortgage companies. In addition, major machinery purchases are often being financed by the captive finance companies of the manufacturer. Just as many people find it convenient to finance a car with the manufacturer, at the point of sale, farmers are taking advantage of similar conveniences when purchasing tractors, combines, and other essential equipment.

Shifting public emphasis coupled with increased competition suggests that traditional lenders must make adjustments in order to maintain and expand their customer base. As a financial institution that is heavily involved in and focused on its community, FNB-Shelby determined to develop products and services that would give its customers more options and support the agricultural industry in the area.

In this new environment, FNB-Shelby recognized a need for comprehensive technical assistance, particularly for small or first-time farmers. FNB-Shelby's management indicated that in the late 1980s many financial institutions in the area focused on large borrowers and depositors. But it was often the small farmer, who generally wanted less than $150,000 in financing, who needed flexible lending instruments and extensive technical assistance. FNB-Shelby, the only bank located in Shelby, has taken a hands-on approach to lending to small farmers who may be very good at farming but may lack the technical and analytical expertise necessary to ensure maximum profitability of the business.

[2] U.S. Dept. of Agriculture, "1996 Farm Bill Fact Sheet," April 1996.

Best Practice Program or Product

Historically, FNB-Shelby has provided a limited line of short-term agricultural loan products to its customers. The Bank's agricultural loan portfolio consisted of loans for livestock purchases, crop production, equipment purchases and repairs, and administrative operating loans. These loans were typically one-year renewable lines of credit. However, beginning in 1992 FNB-Shelby made a concerted effort to diversify its loan products to meet the needs of small farmers in the community. Diversification required that the Bank take a full inventory of its loan portfolio and develop a strategy for extending additional credit to borrowers without putting its financial position at risk. A series of lending initiatives were undertaken and are described below.

As FNB-Shelby became more committed to agricultural lending, it became essential to establish new funding sources. As it turned out, the Federal Home Loan Bank of Topeka ("FHLB-Topeka"), had a number of products that the Bank could take advantage of for managing its liquidity position. The cyclical nature of agricultural lending makes sound liquidity management essential. A community bank that is loaned out during peak seasons will be unable to truly serve the needs of its community. Situations like that will force farmers to seek funding elsewhere. The Bank pledged its residential mortgage loan portfolio as collateral, enabling it to secure $2.2 million in revolving credit from the FHLB-Topeka.

With the availability of funds from the FHLB-Topeka FNB-Shelby was able to make more loans to its customers and further stimulate economic growth in the community. Although the FHLB-Topeka program does not require lenders to track or report loan activity, the Bank estimates that $1 million of the initial revolving line of credit has been extended to borrowers in the form of automobile loans, agricultural loans and real estate loans. FNB-Shelby's president credits the FHLB-Topeka's program with providing the Bank just the liquidity management tool necessary, at the right price, to enable the Bank to be more responsive to the needs of the community.

Another popular initiative for the Bank has been the First-Time Agricultural Real Estate Land Buyer Program ("Land Buyer Program"). In 1993, FNB-Shelby joined with the Nebraska Investment Finance Authority ("Finance Authority") and the Farm Service Agency to deliver affordable agricultural land purchase loans to first-time buyers. The Land Buyer Program is designed to encourage first-time farmers and ranchers to invest in the agriculture industry and economic development of the community.

The Land Buyer Program is primarily used to finance land purchases for agricultural production, such as crops and livestock. The major requirements of the Land Buyer Program mandate that the borrower (i) be a first-time agricultural land buyer; (ii) have less than 10 years experience as a farmer or rancher; (iii) have net worth of less than $250,000; and, (iv) be substantially involved in farming the land. While the property financed using the Land Buyer Program may include a house, the value of the house may only account for 30 percent of the appraised value of the total property.

Each Land Buyer Program transaction requires three sources of financing. The borrower provides 10 percent of the purchase price as a down payment. Thirty percent of the financing is supplied through a direct loan from the Farm Service Agency, which receives a second lien position. The Farm Service Agency may charge a preferential interest rate of not less than 4 percent.[3] As the lead lender, FNB-Shelby funds the remaining 60 percent and obtains the first lien position. Once the loan is closed, FNB-Shelby swaps the loan for a partially tax exempt bond from the Finance Authority. The terms of the bond are identical to the terms of the loan, and the loan proceeds are the source of repayment for the bond. The tax exempt status of some of the proceeds of the bond enable the Bank to offer a reduced rate on the loan while still earning a market rate of return on the entire transaction. The Bank currently offers a 30-year loan with a 10-year fixed interest rate of 6.25 percent. After the first 10 years, there is an adjustment feature that will increase the rate of interest to 25 basis points over the national prime rate.

In 1998, FNB-Shelby became active in originating agricultural loans for the secondary market utilizing an agreement with the Federal Agricultural Mortgage Corporation ("Farmer Mac"). The Farmer Mac agreement is important to the Bank because it (i) expands the Bank's loan products, and (ii) gives FNB-Shelby the flexibility to portfolio agricultural loans or package them for the secondary market. Currently, Farmer Mac is purchasing three loan products from its participating lenders:

1) A 15-year fixed rate product with a 15-year maturity.
2) A 5-year reset rate product that adjusts in five years to a new Farmer Mac 5-year rate.
3) A 1-yearTreasury ARM Product with a 15-year maturity. This product has a lifetime cap of 6 percent over the initial rate.[4]

Similar to the residential secondary market, FNB-Shelby derives fee income from the origination of loans sold to Farmer Mac. The major underwriting difference between a Farmer Mac loan and a conventional residential mortgage is that lenders may use both the adjusted gross income and the depreciation amount on the federal income tax return Schedule Form F[5] to determine the borrower's income.

In addition to offering new loan products, FNB-Shelby is focusing on the growing need to provide more technical assistance to all borrowers both before and after loans are made. For small farmers, understanding changes in the economic landscape, diverse financial instruments and banking services can be intimidating. FNB-Shelby's management believes that providing comprehensive technical assistance to their borrowers is a key component in the success of their lending programs.

Realizing how critical technical assistance can be, FNB-Shelby loan officers are trained and encouraged to focus on educating the borrower; walking him or her through the entire loan process before a loan is made. Technical assistance offered by the Bank may include financial statement analysis, cash flow projections, and tailored financing to meet the needs and abilities of the borrower. After a loan is made the Bank continues to provide technical assistance in an effort to reduce the likelihood of default. To date, FNB-Shelby has been successful in minimizing its losses in part because of the careful post-closing monitoring it does.

[3] Farm Service Agency loans are currently being made for 10 years at 4 percent interest.
[4] Western, Doane. "What is Farmer Mac: Farmer Mac Real Estate Loans." <http://www.avicom.net/doane/page2.hmll> Online. Internet. 26 Mar. 1998.
[5] The profit and loss statement form.

EXPERIENCES AND OBSTACLES

With the presence of an agricultural secondary market, the Bank has an opportunity to offer more financial options to the consumer. Year-to-date, FNB-Shelby has three Farmer Mac loans in the "pipeline" and is optimistic about the potential of the relationship and its ability to make the Bank competitive with other financial services providers in the area.

The Land Buyer Program is an important initiative for the Bank because it has the helped young borrowers with limited experience and assets become farmers and FNB-Shelby customers. For example, FNB-

Financed by the FSA's Beginning Farmer Program and NIFA, this 75 acre ranch was purchased by one of FNB's young farmers.

Shelby recently helped a young farmer purchase 75 acres of undeveloped farm land in Rising City, NE. The purchase price for the land, which will be used to grow crops, was $150,000. He will farm his 75 acres, along with 400 adjacent acres that he is currently renting, in order to achieve profitability. There is an enormous potential to develop this and similar borrowers at an early age and service their accounts as they grow.

There is a strong need to educate the borrower through training and technical assistance.

Many of the smaller or first-time borrowers may not have the expertise needed to manage the business side of their farms profitability. Therefore, the Bank has placed a significant emphasis on educating the borrower regarding its products, programs, and issues that may effect their business. Developing a comprehensive in-house technical assistance program has been a plus for the Bank because it has enhanced their client relationships and allowed FNB-Shelby to focus on these accounts more frequently.

Current Status

Overall, the Bank's venture into agricultural lending has paid significant dividends. Since 1992, FNB-Shelby has made 335 agricultural loans totaling almost $14 million. Additionally, its approach to customer service and focus on providing customers with comprehensive technical assistance have been equally successful. Since, 1992 the Bank has not recorded a default on an agricultural loan.

Partnerships

The following entities have cooperated and partnered with FNB-Shelby to deliver affordable capital and competitive products to borrowers: The Federal Home Loan Bank of Topeka, Nebraska Investment Finance Authority, Farm Services Agency, and Farmer Mac.

ADDITIONAL INFORMATION CONTACTS

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USDA Facilities Locator:
http://offices.usda.gov
Rural Development Field Offices:
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MUNICIPAL LENDING

The Howard Bank, NA

PARTICIPANT PROFILES

Howard Bank is a national bank in Burlington, Vermont. The Bank has approximately $688 million in total assets and is a dominant regional institution with 13 branch offices in 4 counties. Its business is a mix of commercial, real estate and personal loans. At the end of 1997, the Bank had $482 million in loans with deposits totaling $531 million. Nearly 70 percent of the loan portfolio is commercial, while 65 percent of its deposits are retail. The Bank also has an active consumer, installment and credit card operation.

Howard Bank is heavily involved in equity investments in community development corporations ("CDC") in Vermont. These investments have provided funding for various housing and economic development initiatives. In 1989, the Bank received special approval from the OCC to invest in limited equity partnerships with CDCs. At that time, Howard Bank was the only national bank to request and receive approval for this type of investment.

In recent years, Howard Bank has directed its efforts toward municipal and community reinvestment lending. The Bank's municipal lending programs are the subject of the Best Practices focus of this paper. Howard Bank's unique lending programs have been successful for the Bank while providing its communities with an important partner for community development initiatives. Howard Bank has developed a solid reputation in its local markets as an innovative partner in strengthening communities through creative, yet sound lending practices.

COMMUNITY BACKGROUND

The state of Vermont is largely rural, with a total population of 585,000 in 1995.[1] The state is nationally known for its fall foliage and winter skiing, making tourism very important to the state's economy. Howard Bank serves two distinct markets, the urban market consisting of Chittenden County and the more rural market consisting of Washington, Orleans and Caledonia counties. All four counties are in the northern and central parts of the state.

Chittenden County has Vermont's greatest population density and includes the state's largest city, Burlington. In 1995 the population of the county was 139,000, 24 percent of the state's total population.[2] Chittenden County also is the most important economic center in Vermont. In 1995, its median household income was $36,877, while the unemployment rate was only 3 percent.[3] Major sources of employment include an IBM microchip manufacturing plant, a large regional health care provider, four small colleges and the University of Vermont. A strong presence of sales and service related companies, as well as financial service providers rounds out the Chittenden County economy.

Washington, Orleans, and Caledonia counties each have much smaller populations and are more rural than Chittenden County. In 1995, these counties had a combined population of about 109,000 and the median household income was $25,807. Employment is slightly higher and housing prices slightly lower than Chittenden County. Local agricultural and logging activities are the chief employers in the area.

[1] Vermont Population Projections: 1990-2015, Vermont Health Care Authority, Center for Rural Studies, June 1993.
[2] Vermont Population Projections: 1990-2015, Vermont Health Care Authority, Center for Rural Studies, June 1993.
[3] Vermont Department of Economic Development.

COMMUNITY NEEDS

The development and viability of the rural towns and villages are dependent upon access to affordable financing. The financial institutions in Vermont provide credit to fund a significant portion of the current expenses incurred and improvements made by these municipalities.

The municipalities need both short-term and long-term financing. Capital improvements such as construction of schools and the purchase of equipment like fire engines and police cars are generally financed with long-term credit. Short-term needs are generally caused by the mismatch between cash collections and expenditures. For example, taxes may be collected on a semiannual basis, while expenses are incurred daily. Credit to even out these cash flow problems is essential to meet municipalities' needs.

Howard Bank has been extending credit to municipalities, which for purposes of this paper is defined to include school districts, towns and other political subdivisions, for over 15 years. From a small beginning, Howard Bank has responded to demand and opportunity by expanding its municipal banking operation, adding a broad array of credit products and banking services. Howard Bank is now a key player in the small community municipal lending arena.

Howard Bank believes that municipal finance not only meets its profit objectives, but also represents a growing niche market. As the federal government transfers greater economic decision making powers to local jurisdictions, municipal needs are growing and diversifying. Howard Bank's senior management believes that municipalities will continue to need new products and services and that banking relationships with municipalities will continue to comprise a significant portion of their business for the foreseeable future.

BEST PRACTICE PROGRAM OR PRODUCT

In 1994, Howard Bank created a separate municipal lending department that focused on developing specific products and services to meet the needs of this market. The Bank recognized five important benefits from the development of a strong municipal lending presence in rural Vermont: (i) municipal investments were part of its commitment to community development; (ii) municipal lending could be incorporated into its CRA portfolio; (iii) providing municipal banking services was a profitable business; (iv) municipal loans represented relatively low-risk investments; and (iv) municipal lending created an opportunity to cross sell other deposit and cash management services.

Most municipal loans are relatively low risk. In Vermont, typically municipal loans are the "general obligation" of Vermont towns, villages, town school districts, and union school districts. As such, they are backed by the full faith and credit of the municipality. Furthermore, in Vermont, the municipality has the power and authority to raise taxes to meet its financial obligations, and is required to do so by law. 24 V.S.A. §§ 1751, 1898.

Another important benefit of municipal lending is its potential tax benefits to a financial institution. In general, municipalities issue tax-exempt notes for various financing purposes. Interest income from the notes is typically tax-exempt. In addition, Howard Bank is allowed to deduct 80 percent of the interest expense associated with funding these assets if the transaction meets the requirements of the IRS Code. In order for the Bank to qualify for this treatment under the Tax Code the borrowing municipality must meet certain criteria that includes, most importantly, not issuing more than $10 million in qualifying debt in a calendar year.

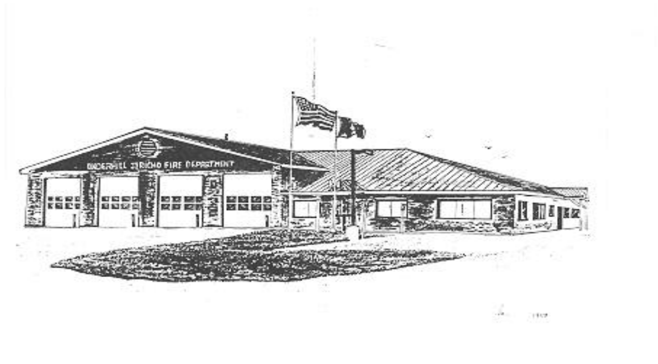
All municipalities have ongoing funding needs that include managing cash flow, balancing the fiscal budget, purchasing new equipment, and financing improvements in infrastructure. Typically, the following financial instruments are used to provide short-term financing:

- *Tax Anticipation Notes*: issued in anticipation of tax revenues to be received during the fiscal year.
- *Bond Anticipation Notes*: issued in anticipation of the sale of municipal bonds.

- *Grant Anticipation Notes*: issued for projects to be paid for by federal or state funds.
- *Capital Improvement Notes*: issued to finance construction projects and equipment or vehicle purchases.
- *Highway Equipment Notes*: issued to finance the purchase of highway equipment.
- *Current Expense Notes*: issued to finance other legal borrowings not covered by other products (e.g. school district financing).

Tax Anticipation Notes are some of the most popular financing instruments for municipalities because there are no monthly payments. Municipalities may draw against the loan as needed, while the bank provides the account management services. The terms for these loans are principal and interest due at maturity. According to Howard Bank management, municipal loans generally should be priced to achieve at least a 1.5 percent pre-tax spread. Howard Bank's current terms are less than 1 year at 4.5 percent.

Municipal Equipment Notes are another attractive form of municipal lending. This type of financing is essential to small communities whose budget cannot meet unexpected equipment needs or emergencies. For example, in 1996, the Bank lent $55,000 under a Highway Equipment note to the Town of Bolton to purchase a 1996 dump truck for snow removal and other municipal purposes. The loan was for one year, with a five-year amortization. The pricing was competitively bid at 4.3 percent and an annual rate adjustment with each renewal. Bolton town officials expect to retire the debt prior to full amortization.



The above rendition of the Underhill-Jericho Fire Station, located in Chittenden County, VT was financed by the Howard Bank. The total cost of the municipal construction loan was $500,000.

Municipal Equipment Notes are usually financed with a five-year adjustable rate product whose rate is tied either to the Federal Home Loan Bank index, the LIBOR, or the prime rate. Monthly payments or other terms are set up at the customer's request and for their convenience only.

In addition to designing new products, municipal lending requires the establishment of special underwriting criteria. Underwriting guidelines for municipal loans are not as complex as some other forms of commercial debt primarily because most of these loans are short-term notes that are made in anticipation of annual municipal funding and collected on or prior to the note maturity date, making them essentially self-liquidating. The vast majority of municipal loans underwritten by the Bank have a maturity of one year or less. The reduced risk associated with these loans as a result of Sections 1751 and 1898 of the Vermont statutes, which grant municipalities the right to raise taxes in order to satisfy general obligations, as well as the short term length have allowed Howard Bank to set up flexible underwriting criteria for its municipal customers.

In recent years, municipal treasurers have become much more knowledgeable about investing and maximizing the return on the investment of taxpayer dollars. To attract these investment dollars Howard Bank has designed specialized depository products to meet the asset protection and investment needs of municipalities. One such product is their Deposit Collateralized Protection Program. Under this program municipalities may elect to secure additional insurance on deposits not covered by the $100,000 FDIC guarantee. The Bank provides the additional deposit insurance through a third party insurer, Municipal Bond Investment Assurance Corporation ("MBIA").

MBIA was selected on the basis that the company would provide Howard Bank additional insurance coverage for up to $12 million in total municipal deposits. MBIA charges the Bank nominal rates, generally between ¼ to ½ of 1 basis point, for the coverage. The cost of this additional insurance is passed on to the municipalities that receive the coverage. This program is an innovative way to protect public funds by purchasing additional insurance while still serving Howard Bank's interest in managing large municipal deposits.

The Bank also offers "sweep accounts" on demand deposits that provide additional income to the municipality when the accounts are swept and the excess is invested in overnight instruments. Through this program, Howard Bank is able to offer high returns on deposits at minimum risk. By automatically "sweeping" and investing overnight checking account balances, the Bank may make temporary purchases of government or government agency securities on behalf of the municipality. Then the bank agrees to repurchase the securities, usually the very next day. This product provides the depositor with the liquidity and return it needs and wants, as well as the collateral protection necessary to safeguard public funds. This product has been very attractive to Howard Bank's municipal customers.

EXPERIENCES AND OBSTACLES

The relatively small communities and limited resources make municipal lending a challenge in Vermont. Historically, Vermont banks have made deposit services complimentary for their local municipal customers in exchange for large non-interest bearing balances. However, over the last decade, Vermont municipalities have experienced an increased awareness of how to invest excess cash to maximize interest potential. Municipal treasurers also have become more cognizant of the financial strength of insured depositories.

Various municipal organizations have attempted to educate their members about banking relationships and tried to provide recommendations for prudent management of the public funds. These efforts have increased the level of municipality expertise in these areas, which has in turn presented new opportunities for Vermont banks. The Howard Bank has worked with dozens of community leaders to meet the new needs of the municipalities.

Despite the progress made by the various municipal organizations, there still appears to be a significant opportunity for educating those responsible for municipal funds on the various banking services available to them. The Howard Bank has expended significant resources assisting local governments with the wide variety of financial services that can be helpful in managing their cash flow. For instance, in the past year, Howard Bank has successfully introduced lockbox and automated clearinghouse services to several municipalities that had not known about these services. Howard Bank has found that a strong cash management product line builds a solid banking relationship with its municipal customers.

The Bank established its municipal lending department as a self-funding operation from the outset, without funding a separate department budget, to give staff the incentive to make the department self supporting from the beginning. This self funding goal was accomplished through lending and cross-selling bank products to the municipal customers. The newly created department was generating significant revenues for the Bank by the end of its first year of operation.

Howard Bank also markets its municipal products extensively. Representatives from the Bank attend a variety of municipal functions and maintain exhibits at area trade shows. These activities have helped increase the Bank's visibility and demonstrate its commitment to the market.

CURRENT STATUS

In 1994, its first full year of municipal lending, Howard Bank made 59 loans totaling $9 million. The development of additional products and services has allowed the Bank to expand their municipal business by 368 percent over the last 3 years.

PARTNERSHIPS

Howard Bank has assisted many cities, towns, and villages, as well as various school districts and other municipal entities with their financial needs. Additionally, the Bank has partnered with organizations, such as MBIA to provide a full line of services to its depositors.

ADDITIONAL INFORMATION CONTACTS

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ADDITIONAL RESOURCES

Center for Rural Studies
207 Morrill Hall
University of Vermont
Burlington, Vermont 05405
Phone: (802) 656-3021
http://crs.uvm.edu/

Department of Housing and Community Development
State of Vermont
National Life Building
Drawer 20
Montpelier, Vermont 05620-0501
http://www.state.vt.us/dca/housing

CAPACITY BUILDING

Sturgis Bank & Trust

PARTICIPANT PROFILES

Sturgis Bank & Trust ("Sturgis Bank") is a federally charted savings bank located in Sturgis, Michigan, with assets totaling approximately $200 million. While Sturgis Bank offers a variety of non-mortgage products such as auto, home equity and commercial loans, as well as credit cards, its primary focus, mortgage lending, constitutes 89 percent of its total loans. Sturgis Bank offers a variety of mortgage loan products, including FHA, VA and Rural Housing Services insured loans, to its customers and is the number one mortgage originator in St. Joseph County.

Sturgis Bank has been a leader in promoting affordable housing for low- and moderate-income families. In addition to Sturgis Bank's initiative designed to build the capacity of non-profit organizations to assist more clients with more services that is featured below as the Best Practice portion of this paper, Sturgis Bank also is the only local financial institution to use the U.S. Department of Agriculture's ("USDA") Section 502 Loan Program. Through the use of this program, Sturgis Bank is able to be more flexible in underwriting loans to low- and moderate-income families and first-time home buyers. During 1995 and 1996, Sturgis Bank originated 93 loans totaling $4.1 million dollars using this program.

COMMUNITY BACKGROUND

Sturgis Bank's primary lending market is in St. Joseph County, the area in which six of the its eight branches are located. According to 1990 Census data, the total population of St. Joseph County at that time was 58,913. The median housing value in the area was approximately $44,800, with a median age of 38 years. The U.S. Census Bureau estimates that as of July 1, 1997, the total population of St. Joseph County rose to 61,234.

The major source of employment in St. Joseph County is the private sector, with the manufacturing business accounting for the highest number of jobs. The major employers in the area are manufacturing companies such as Cooper Industries, Ross Labs, Grumman Olson, and Burr Oak Tool and Gauge. Local economic conditions have generally been positive. In 1995, the unemployment rate averaged approximately 3.5 percent.[1]

Sturgis, a town with a population of 10,310, depends upon the manufacturing industry for jobs. Manufacturing plants supply the community with more than 5,000 jobs. The importance of manufacturing to the local economy is evidenced by the fact that 15 of the 19 local employers with 100 or more employees are manufacturing entities. A total of 4,600 jobs, or 92 percent of the total manufacturing-related positions, are provided by these 15 companies.

[1] Development Research Associates, Inc., "Housing Market Report - City of Sturgis," (April 30, 1996).

COMMUNITY NEEDS

Sturgis' downtown area has a high concentration of deteriorating and sub-standard housing that was built before 1940. The majority of the downtown residential properties are single-family dwellings owned by absentee landlords and rented to very low-income families. In most cases, these families lack both the financial resources to purchase a home and the basic skills to balance household budgets and maintain their homes.[2] Further, the district had problems with young adults loitering and creating public disturbances.

The Sturgis Chamber of Commerce assembled a committee of community business leaders to address these problems. The committee concluded that the problems were both social and economic and were becoming more commonplace in rural communities. The committee also concluded that the problems were directly related to inadequate housing and a lack of social service programs. The committee's recommendations led to the creation of the Sturgis Neighborhood Program ("Neighborhood Program").

Founded in 1991 as a non-profit entity, the Neighborhood Program took on the challenge of addressing the affordable housing needs of the city's residents, whose incomes were 50-to-80-percent of the area's median. The organizational challenge for the Neighborhood Program was to develop sustainable programs that offered housing services, social and economic support services and property management. However, the non-profit organization lacked the critical financial and technical resources needed to achieve its mission.

[2] Susanne C. Schnell. "Profiles of Partnership Achievements: Street Tested Strategies for Strengthening Neighborhoods." The Social Compact. 1997. P. 124.

Best Practice Program or Product

In 1991, Sturgis Bank became the first local lender to actively support the Neighborhood Program's effort to promote property rehabilitation and tenant self-reliance. Sturgis Bank realized that it was essential that the Neighborhood Program have the expertise and resources needed to renovate dilapidated housing and provide tenants with mentoring and social services. Therefore, it spearheaded an initiative to build the Neighborhood Program to meet these objectives. Through the proactive efforts of Sturgis Bank's president and management team, the Neighborhood Program has been supplied with planning assistance, mortgage training, technical assistance and financial resources at crucial stages of its development. Sturgis Bank has worked diligently behind the scenes to encourage other lenders to support the Neighborhood Program's community development efforts. For example, KeyBank, FSB, also located in Sturgis, has donated office space and utilities to the program. Sturgis Bank continues to actively participate in many facets of the Neighborhood Program's operation and has representatives on its project, finance, public relations, and advocacy committees. The Neighborhood Program's current President is Tracy Parker, a Vice President and CRA officer at Sturgis Bank.

The Neighborhood Program administers its projects by providing advertising, outreach, pre-application screening, and budget and credit counseling. The Neighborhood Program also works closely with its established tenants to provide home maintenance training, personal financial management and parenting workshops. All project tenants must actively participate in setting and achieving family-improvement goals that are agreed upon by the Neighborhood Program and the families. The tenants must agree to maintain the interior and exterior of the properties they rent from the Neighborhood Program. Failure to comply with the goal setting program and property responsibilities can result in termination of the tenant's lease.

The main purpose of the tenant agreement is to ensure that the families remain in the program and improve the quality of their lives. Through this agreement the Neighborhood Program administers various comprehensive programs, such as peer counseling, social support services, home ownership education workshops, budget and credit counseling and employment counseling.

Like most non-profit organizations, the Neighborhood Program lacks the paid staff to effectively conduct all of the one-to-one counseling that is needed. In an effort to supplement the services they are offering and to assist their tenants in becoming functioning members of their new community, the Neighborhood Program developed a community mentoring program. Under this program, volunteers from the community act as mentors to the Neighborhood Program's tenants. A critical feature of the program is that each client must meet with his/her mentor once every 60 days. These meetings serve at least two important purposes. First, they enable and encourage individuals from different cultural and ethnic backgrounds to develop closer relationships. Second, the mentor program gives the Neighborhood Program staff an early indication of how likely particular tenants are to fulfill all the terms of their agreement. The Neighborhood Program staff has found that tenants who are successful in the mentor program generally complete the other portions of the program successfully.

In addition to the financial assistance outlined below, Sturgis Bank holds first-time home buyer seminars on a quarterly basis. The program includes realtors, insurance agents, attorneys, and home inspectors. The seminars focus on the mortgage application process, loan products, down payment and closing cost requirements. Sturgis Bank offers monthly budget and credit counseling classes, as well.

In 1991, Sturgis Bank's Board of Directors approved a $200,000 line of credit for the Neighborhood Program with interest equal to its cost of funds, plus one percent. InExperiences and Obstacles
addition to the below market interest rates, Sturgis Bank applied flexible underwriting standards. These funds were used by the Neighborhood Program to purchase and renovate dilapidated properties in the community. In 1997, Sturgis Bank increased this line of credit to $300,000.

In 1995, with the assistance of Sturgis Bank, the Neighborhood Program was awarded $69,000 by the Federal Home Loan Bank of Indianapolis. The money funded the renovation of three single family homes and two duplexes that are currently fully rented. Also in 1995, the Neighborhood Program won a Michigan State Housing Development Authority ("Housing Authority") grant of $200,000. The grant paid for the renovation of several existing Neighborhood Program properties and for the purchase and rehabilitation of two additional homes in the city. Twenty thousand dollars was designated for administrative expenses. Currently, all of the units are occupied with families whose incomes are 50-to-60 percent of the local median, a Housing Authority requirement.

EXPERIENCES AND OBSTACLES

The Sturgis Bank line of credit described above has been used by the Neighborhood Program to acquire and rehabilitate distressed properties that are then leased or sold to qualified applicants. For example, one property needed a complete interior renovation and certain structural modifications. The Neighborhood Program purchased the property for $17,000 and completely renovated the home. Today, the property is appraised at $55,000, and the four bedroom unit is home to a family of six. The family, whose income is half the local median, pays $385 a month in rent.

Over the past seven years, Sturgis Bank has consistently provided funding to help cover t the Neighborhood Program's operational and administrative expenses. It contributes a minimum of $2,000 a year toward the Neighborhood Program's operational expenses. In addition, Sturgis Bank sponsors an annual golf tournament to raise funds for the non-profit organization. The tournament, which began last year, attracted 100 participants and raised $5,500. These funds are primarily used to fund some of the Neighborhood Program's social support programs for the community. The Neighborhood Program management credits Sturgis Bank's commitment to their program, as well as Sturgis Bank's efforts to involve other financial institutions and other non-profit organizations as "the driving force" that has made the Neighborhood Program successful. Currently, Sturgis Bank has several employees actively involved with the Neighborhood Program. For example, the Bank's President and a Senior Vice President serve on the Neighborhood Program's Board of Directors and one employee serves on the Neighborhood Program finance committee. This support assisted the Neighborhood Program in overcoming what is often the biggest obstacle to the formation and capacity building of a non-profit organization in rural areas – finding entities with both the will and the capacity to foster the development of a fledgling non-profit organization.

CURRENT STATUS

The Neighborhood Program has successfully established itself as an important force in the town of Sturgis. Through its initiatives, low- and moderate-income families can afford adequate housing and develop self-reliance skills that will make them more productive members of the community. By publicly partnering with the Neighborhood Program in its community development initiatives, Sturgis Bank lent credibility to the non-profit that was critical to its ultimate success and acceptance in the community.

This property was purchased and rehabilitated by the SNP. The home was later sold to a family who successfully completed the mentoring program.

To date, the Neighborhood Program has purchased and rehabilitated seven housing units (four single family and three duplexes), that are rented to qualified families with incomes that are 50 to 60 percent of the area's median. The Neighborhood Program has renovated and sold two properties to low-income families. A third renovated home is being sold to a former Neighborhood Program tenant. Sturgis Bank holds the mortgages on five of those properties.

In its most ambitious project yet, the Neighborhood Program is working with Reenders Inc., a local developer, to build Eastwood Village. The project will create 80 low- and moderate-income units on a 10-acre site located on the east side of Sturgis. The multi-unit facility will include 50 single family townhomes for low-income families and a 30-unit apartment building for senior citizens. Additionally, architects have designed the facility to include a community room and an on-site child-care facility. The Neighborhood Program also may relocate to an office at the complex. Monthly rents are expected to be $350 for one-bedroom units, $420 for two-bedroom units, and $485 for three-bedroom units. The annual income for a family of four would be approximately $23,000 and for an elderly couple, $18,000. Sturgis Bank is serving as a financial consultant to the Neighborhood Program on this project.

Funding for the project will come from the Housing Authority or similar financing and tax credit equity. The use of tax credits will allow local banks and businesses to help finance the project by purchasing the credits. The goal is to break ground in the fall of 1998 and have the project completed by the spring of 1999. Eastwood Village is significant in that it is the first multiple unit development for the Neighborhood Program.

PARTNERSHIPS

Sturgis Bank has worked closely with the Sturgis Neighborhood Program, the Sturgis Chamber of Commerce, the City of Sturgis, the County of St. Joseph, Federal Home Loan Bank of Indianapolis, the Michigan State Housing Development Authority, USDA Rural Development, local lenders, attorneys, and community residents.

ADDITIONAL INFORMATION CONTACTS

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Fax: (616) 651-5512

U.S. Department of Agriculture
14th & Independence Ave. SW,
Washington, D.C. 20250
Phone: (202) 720-2791
Main Web Site: www.usda.gov
USDA Facilities Locator: offices.usda.gov
Rural Development Field Offices:
www.rurdev.usda

ADDITIONAL RESOURCES

Michigan State Housing Development Authority
401 S. Washington Square
Plaza One Building
Lansing, MI 48909
Internet Home Page: http://www.voyager.net/mshda/

Rural Development Directory

This directory includes all those individuals and entities upon whom the OTS relied in developing our research for this paper. It is an impressive assortment of lenders, community-based organizations, individuals, national intermediaries, government sponsored entities, and federal, state and local government agencies. We are grateful to them all for their assistance.

Alternative Federal Credit Union
301 West State Street
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Mr. Bill Meyers
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Regional Community Development Financial Institution.

American Banking Company
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Mr. Ronnie Marchant
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(912) 985-2828 Fax
Community Bank.

America's Community Bankers
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Washington, DC 20006
Ms. Charlotte Bahin
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(202) 857-3121
(202) 296-8716 Fax
Association of more than 1,500 Savings and Community Financial Institutions.

American Home Ownership Education Counseling Institute
Suite 1220, 1156 15th Street, NW
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Ms. Karen Hill
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(888) 243-2499
(888) 243-2477 Fax
National Housing Counseling Institute.

Aspen Institute
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Mr. Meriweather Jones
Executive Director
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(202) 467-0790 Fax
Ms. Diane Morton
Rural Economic Technical Assistance and Policy Organization.

Association of Farmworker Opportunity Programs
Suite 910, 1611 North Kent Street
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Ms. Lynda Diane Mull
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(703) 528-4145 Fax
National Employment, Training, and Support Services Organization.

Association of Local Housing Finance Agencies
Suite 300, 1200 19th Street, NW
Washington, DC 20036
Ms. Susan Ellis
Housing Finance Director
(202) 857-1997
(202) 857-1111 Fax
National Non-Profit Association of Affordable Housing Finance Professionals.

Bank of America
500 N. Akard Street, 23rd Floor
Dallas, TX 75201
Mr. James Richardson
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(214) 758-4658
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Community Development Department.

Bay Meadow Corporation
2310 North Patterson Street, Bldg. H
Valdosta, GA 31620
Ms. Emily Hagan
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(912) 245-8774
(912) 245-0570 Fax
Local Affordable Housing Developer.

Border Waterworks
1227 Paseo De Peralta
Santa Fe, NM 87501
Mr Charlie Clemments
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(505) 988-4270
(505) 984-3089 Fax
Regional Water Self-Help Organization.

Butler & Associates
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Ms. Pat Butler
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Rural Development Consulting Firm.

Center For Community Change
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National Technical Assistance Non-Profit Organization.

Center for Community Self Help
301 West Main Street
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(919) 956-4600 Fax
Statewide Community Development Non-Profit.

Center For Economic Options
601 Delaware Avenue
Charleston, WV 25302
Ms. Pam Curry
Executive Director
(304) 345-1298
(304) 342-0641 Fax
Regional Economic and Microbusiness Development Organization.

Center For Rural Affairs
P.O. Box 406
Walthill, Nebraska 68067
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(402) 846-5428
(402) 846-5420 Fax
Private Non-Profit Research Organization.

Central Appalachian Peoples Credit Union
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Rural Development Division.

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Mr. Ron Phillips
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Statewide Community Development Corporation.

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(303) 620-4789 Fax
State-Sponsored Rural Technology Development Program.

Community Equity Investments, Inc.
302 North Barcelona Street
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(850) 595-6234
(850) 595-6264 Fax
Regional Small Business Development Non-Profit.

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Raleigh, NC 27619-1999
Mr. Roger Earnhardt
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(919) 881-9909 Fax
Statewide Consortium.

Community Works in West Virginia
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Ms. Lynn Talley
Executive Director
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Statewide Non-Profit Housing Consortium.

Dept. of Housing and Urban Development
Office of Consumer and Regulatory Affairs
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Washington, DC 20410
Ms. Marion F. Connell
Director
(202) 708-6409
(202) 708-4213 Fax
Manufactured Housing and Standards Division.

Dept. of Housing and Urban Development
Single Family Development
75 Spring Street, SW
Atlanta, GA 30303
Mr. Ralph Jackson
Manager, Single Family Products
(404) 331-4801 Ext 3153
(404) 730-3152 Fax
Regional Office.

Enterprise Corporation of the Delta
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