



July 26, 2010

Branch Chief  
Regulations and Paperwork Management Branch  
U.S. Department of Agriculture  
Via Federal eRulemaking Portal: [www.regulations.gov](http://www.regulations.gov)

Re: Comments on Proposed Rule 7 CFR 4280, Rural Microentrepreneur Assistance Program

Pursuant to the Proposed Rule for the Rural Microentrepreneur Assistance Program (RMAP), 7 CFR 4280 published May 28, 2010, the Corporation for Economic Development (CFED) submits the following comments:

CFED greatly appreciates the United States Department of Agriculture's (USDA or "the Agency") publication of the Interim Rule that would implement the 2008 Rural Microentrepreneur Assistance Program. We commend the considerable work of the Agency staff to develop this proposed rule, and also thank them for their open communications with those interested in and supportive of microenterprise.

CFED is a national nonpartisan, nonprofit organization dedicated to expanding economic opportunity. We believe such economic opportunity will bring greater social equity, alleviate poverty and lead to a more sustainable economy. As a leader in economic development for nearly three decades, CFED collaborates with diverse partners at the national, regional, state and local levels. We bring together community practice, public policy and private markets in new and effective ways.

Our comments address several areas of the Interim Rule, and we look forward to working in partnership with USDA to continue to strengthen RMAP for entrepreneurs and the microenterprise development field.

Note: All references below to "the law" or "the statute" refer to section 6022 of the *Food, Conservation, and Energy Act of 2008* (P.L. 110-246). All references to "report language" refer to H.Rept.110-256 Sec.367.

## 1. Paperwork Reduction Act

The Abstract portion of the Paperwork Reduction Act paragraph states that the term of a microloan to a microentrepreneur will "... not exceed 20 years..." This appears to be a typo, as all other areas of the Interim Rule identify microloans to microentrepreneurs as having 10-year terms. We recommend that USDA ensure clarity of 10-years in the Final Rule.

## 2. Definitions

CFED is pleased to see that USDA has abandoned the need to prove "outmigration" in order to qualify a rural area, although we remain concerned that a strict definition of "outmigration" may yet be applied to future components of RMAP (i.e. "Enhancement Grants," on which USDA is requesting comment).

### § 4280.302(a) Definition of Rural Microloan Revolving Fund (RMRF)

USDA should clarify that it will not hold first lien on any portion of the RMRF that is capitalized with non-Federal funds. Microenterprise practitioners already face an extremely difficult fundraising environment; it will be quite challenging for any microenterprise development organization (MDO) to approach banks and other potential non-Federal contributors without the availability of a first lien position on funds invested. We would like to re-emphasize that USDA should retain first lien position only on the Federally funded portion of the RMRF.

## 3. Administrative Concerns

### Applications by Collaboratives

MDOs often partner to leverage areas of expertise, expand service areas, and lower costs. As such, CFED recommends that the Final Rule allow applications by collaboratives (i.e. statewide microenterprise associations, microenterprise intermediaries, statewide community action agency/programs, etc.) where other eligibility requirements are met.

In particular, the Agency may want to consider assigning a "collaborative/project lead," or requiring collaborative applications to include specific information regarding project and funding liability.

### Division of Funding

The Interim Rule proposes a division of funding that, at maximum, assigns 90% of appropriated funds to the lending portion of RMAP, and 10% of appropriated funds to the technical assistance-only portion of RMAP.

We strongly believe that a more equitable distribution of funding among these categories is essential to ensuring the success of RMAP and of rural microentrepreneurs. Technical assistance is crucial to the success of microenterprise, and the Final Rule should reflect that. CFED proposes the following division of funding:

- 50% for the RMAP loan program;
- 40% for the RMAP technical assistance-only program;
- 10% for an RMAP “enhancement grant” program (discussed further below).

#### § 4280.304 Review or appeal rights and administrative concerns.

To ensure maximum transparency and accountability, the Final Rule should require that USDA respond to applicant reviews and/or appeals within 45 days of receiving such requests.

#### **4. Loans from Agency to Microlenders**

##### § 4280.311 Loan provisions for Agency loans to microlenders.

We strongly disagree with USDA that interest earnings from loans made to microentrepreneurs should be restricted in any way. Interest earnings are one of the very few, if not only, methods upon which MDOs depend to defer the costs of running a loan fund. This is also especially important because the Interim Rule does not make clear whether technical assistance grants can be used to pay for the administrative expenses of running a loan program. In the “Discussion of Comments,” USDA states that MDOs may use “... up to 10% of the [technical assistance grant] funds to cover MDO administrative expenses for administering the technical assistance grants.” CFED recommends several improvements for the Final Rule:

- The administrative portion of technical assistance grant funds may be used to cover the administrative costs of loan programs;
- Section 4280.311(e)(2) should apply only to interest earnings on the underlying USDA loan to the MDO. Based on experience of grantees at the Assets for Independence program at the Administration for Children and Families within the U.S. Department of Health and Human Services, we note that monitoring interest can be time-consuming and burdensome costing more in administrative effort than the value of the interest;
- For lenders who choose the “RMRF Level” option, USDA should not have jurisdiction over interest earnings of the non-Federally funded portion of the RMRF;
- Codify that interest income from microloans: (a) need not be deposited into the RMRF, and/or (b) may be deposited and withdrawn from the RMRF without restriction.

We also recommend that the Final Rule clarify, for those lenders choosing the “Microborrower Project Level Option,” that an entrepreneur’s equity in their business count towards the 25% non-Federal share. Examples of equity include: a vehicle registered in the name of the business, technology purchased for business purposes, investments in equipment or personal savings.

4280.311(e)(9), Loan disbursement.

4280.311(e)(10), First microloan.

The Interim Rule states that MDOs will be eligible to receive a disbursement of up to 25% of the total loan amount at the time of the loan closing, with additional disbursements available on a quarterly basis. The Rule also states that an MDO must make a loan within 30 days of any disbursement. CFED believes that both of these provisions hamper the loan-making process.

First, the quarterly disbursement of loan dollars is unnecessary. While we understand the Agency’s desire to streamline RMAP by coordinating reporting requirements and loan disbursement, we strongly believe that this is to the detriment of RMAP. We are disappointed that the Agency finds more value in requiring quarterly draw downs for the sake of “...keeping like calendars...” than in allowing MDOs ready access to capital for which they have already applied and been approved. CFED recommends that USDA allow MDOs to draw down funds as needed or, at the very least, on a monthly basis; this would result in a more liquid, nimble microenterprise capitalization process. With the dearth of capital for small business lending, USDA should promote nimble access to finances.

4280.311(e)(12), Satisfactory participation.

The Interim Rule defines “satisfactory participation” as “...a default rate of 5% or less and a pattern of delinquencies of 10% or less.” CFED asks that USDA clarify what is meant by a “pattern of delinquencies.” Does this refer to a specific number of delinquencies within a defined time period? Also, for the purposes of RMAP, how does the Agency define “delinquent?” In the absence of existing clarification, we recommend that “delinquent” be defined as a microloan that is 30 days in arrears. We also recommend that a “pattern of delinquencies” be measured as the percentage of delinquent microloans over any one-year RMAP participation period.

4280.311(e)(15), Agency first lien.

As noted earlier, USDA should clarify that it will not hold first lien on any portion of the RMRF that is capitalized with non-Federal funds. Microenterprise practitioners already face an incredibly difficult fundraising environment; it will be extremely challenging for any

MDO to approach banks and other potential non-Federal contributors without the availability of a first lien position on funds invested.

#### 4280.311(h)(8), Changes in key personnel.

CFED believes USDA oversight of MDO-level personnel decision-making is unnecessary. While we understand concerns surrounding the employment of key, knowledgeable personnel, we believe it is extremely burdensome to require USDA approval before an MDO attains new “key personnel.” In addition, the Interim Rule’s preamble takes an even broader approach by stating that “any changes to key personnel” must be first approved by USDA.

We recommend that USDA strike this requirement in all sections of the Final Rule.

#### Loan Loss Reserve Fund (LLRF)

Lastly, regarding the LLRF, we are very pleased that the “Discussion of Comments” section of the Rule notes that funds in the LLRF can be counted towards an intermediary’s non-Federal share requirement. We ask that USDA codify this in the appropriate section of the Final Rule.

#### § 4280.322 Loans from the microlenders to the microentrepreneurs.

#### § 4280.323 Ineligible microloan purposes and uses.

It is unfortunate that the Interim Rule disallows lines of credit. Entrepreneurs that provide seasonal services, and those whose business needs fluctuate according to other markers, would benefit greatly from a more flexible source of capital like a line of credit. For example, a home air conditioning repair service will typically experience a spike in demand during the hot summer months and might request a small revolving line of credit that would meet their cash flow needs more adequately than a three-year loan. Because of the fluid capital needs of microentrepreneurs, we recommend that the Final Rule allow lenders to offer lines of credit.

### **5. Grant provisions**

#### § 4280.313 Grant provisions.

The Rule stipulates that technical assistance (TA) grants will be awarded annually, based upon 25% of the amount owed from the microlender to the Agency, up to \$100,000. Additionally, “...for organizations that borrow any amount greater than \$400,000, up to

and including \$2.5 million, grants will be calculated as 25% of USDA funds borrowed plus 5% of the total amount of microloans outstanding to borrowers.”

CFED believes that this mechanism is inadequate, and actually works against small-dollar lenders by awarding a larger amount of TA grants to MDOs that make large-dollar loans. The Rule incorrectly assumes a strong correlation between the dollar amount of microloans outstanding to borrowers and the TA required to serve those borrowers.

For example, for lenders that borrow \$400,000 or less (although the same principle applies for organizations that borrow more than \$400,000):

- Organization A borrows \$400,000 and makes eight (8) loans for \$400,000 total. They receive \$100,000 in TA. This is \$12,500 in TA per client.
- Organization B borrows \$200,000 and makes one hundred (100) loans for \$200,000 total. They receive \$50,000 TA. This is \$500 in TA per client.

As illustrated above, an MDO with a larger number of clients requiring technical assistance would actually receive less TA grant dollars than an MDO with much fewer clients.

The Rule goes on to state that “During the first year of operation, the percentage [of TA grant dollars for lenders] will be determined based on the amount of the loan to the microlender, but will be disbursed on a quarterly basis based on the amount of microloans made.” This is somewhat contradictory to the described TA grant mechanism, and extremely vague. The Rule does not clarify whether “...amount of microloans made...” refers to dollar amount or quantity of loans.

Even when accounting for economies of scale, there should be a better method for ensuring that entrepreneurs receive adequate technical assistance regardless of the dollar amount of their loan.

CFED recommends that the Final Rule contain a TA grant distribution mechanism that more adequately accounts for both number of loans made, and loan size.

We also request that the Final Rule clarify the TA grant mechanism for a lender’s second year of operation and beyond.

#### § 4280.313(c) TA-only grants (TAGs).

The Interim Rule states that TA-only grantees will be “... considered successful if a minimum of 1-in-5 TA clients are referred for a microloan and are operating a business within 18 months of receiving technical assistance.” We believe that the proposed ratio is ideal yet not reflective of the operating realities of entrepreneurs and MDOs. In this

recessionary economy, a number of entrepreneurs may seek out services yet not need a loan. CFED is leading an effort to offer free tax assistance to Schedule C (self-employed workers) with the hope to connect them to business assistance services. Many of these entrepreneurs might not need a loan but would benefit from technical assistance. A low ratio will discourage MDOs from extensive outreach and innovative partnerships like ours. We recommend that the Final Rule contain a ratio of 1-in-10 TA clients, and that application scoring also reflect this change.

In addition, we request that the Agency clarify the role that TAG “success” plays in either (a) the receipt of future funding, (b) the re-application process, and (c) overall regulatory enforcement of the RMAP program. We want to promote collaborations where some TAG recipients may partner with others who provide the actual loans.

## **6. Application Scoring**

§ 4280.315 MDO application and submission information.

§ 4280.316 Application scoring.

The Proposed Rule provides points for how closely a MDOs microloan portfolio tracks the demographics of their service area. The history of microenterprise in the United States revolves heavily around serving traditionally underserved markets of entrepreneurs; specifically minorities and women. As such, many MDOs specialize in serving certain traditionally underserved population segments of their service area. We are concerned that this rule would penalize MDOs for reaching out to these populations.

CFED recommends that the scoring structure be altered so that the applications of MDOs that have stated missions to provide services to underserved populations are scored on a positive basis. We understand the Agency’s concern regarding equal and fair credit lending laws, and we do not suggest that MDOs should discriminate among clients. However, underserved clients (for example, refugees, returning prisoners or minority groups) reach out to MDOs precisely because they cannot obtain training and capital elsewhere. It is possible for an MDO to have a client base that is 50% minority whereas their service area is 12% minority, not due to discrimination on behalf of the MDO, but due to the inability of that particular minority group to access entrepreneurial services elsewhere. The Final Rule should not penalize MDOs that have targeted specific underserved populations; the Agency should account for the inability of underserved groups to access capital through traditional means.

## Administrative Expenses

The statute states that not more than 10% TA grants can be used to pay for administrative expenses (Section 6022 (4)(C)). However, the Interim Rule provides points according to how much below 10% an MDO proposes using for administrative expenses, providing zero points for 8 to 10% of the TA grant used for administrative expenses. While we applaud the Agency's attempt to reward MDOs that use significantly less than 10% of grant funds for administrative costs, we believe that this provision ultimately penalizes small, new MDOs. As such, CFED recommends eliminating the point system for MDO proposals on use of TA grant funds.

## Portfolio Management

We were confused by the Agency's response that it "... attempted to provide scoring criteria [for portfolio performance] that could be best addressed by all entities as opposed to numerous criteria that would meet regionally-specific benchmarks." We are unaware of such "regionally-specific benchmarks," and rather believe that there are portfolio performance measures that are commonly used and implemented in the nation microenterprise field.

Specifically, we would like to reiterate the concerns of several commenters:

- While applicants are required to "...enter the total number of your microloans paying on time for the three previous fiscal years." The term "paying on time for the three previous fiscal years" is not defined, and could be interpreted numerous ways, including: the number of outstanding loans that never experienced a late payment over the course of the year, the number of loans that were current at year-end, or the number of loans that paid off as scheduled during the course of the year. However the applicant might define this term, none of the above is a widely accepted measure of portfolio quality in the microenterprise or community development finance industry.
- Applicants are required to "...enter the total number of microloans 30 to 90 days in arrears or that have been written off at year end." There are several issues with this approach. First, it conflates delinquent loans with loan losses, which are typically reported and assessed separately (in part because the commonly-accepted definitions of these measures require different denominators when calculating a percentage value). Second, the measures required in the Rule involve the number of late or written off loans, not the dollar value of those loans. In assessing the level of risk in a portfolio, it is the value of loans at risk rather than the number that is most

significant -- as a delinquent or bad loan of \$40,000 will necessarily pose more risk to a portfolio than a delinquent or bad loan of \$4,000.

- Finally, the Interim Rule does not request information on loans that are greater than 90 days in arrears, but have not yet been written off. These are the delinquent loans that generally pose the greatest risk to the lender, particularly if the lender does not have or adhere to a strict policy and time frame for writing off loans that have become significantly delinquent.

CFED agrees with comments made by the Aspen Institute's FIELD Program that would instead request that applicants provide information for the past three fiscal years on the following three measures:

- Portfolio at risk: defined as the outstanding principal balance of loans with payments greater than 30 days past due, divided by the total dollar amount of outstanding loans, as of the last day of the fiscal year.
- Loan loss rate: defined as the total dollar value of loans declared as written off or nonrecoverable, net of recoveries, divided by the average outstanding value of the portfolio over the course of the fiscal year.
- Restructured loan rate: the dollar amount of all loans that have been restructured, divided by the total dollar amount of outstanding loans as of the last day of the fiscal year.

Note that we believe it is important to examine loans that have been restructured, as well as those that are delinquent and/or written off, because those loans do indicate risk to the portfolio.

### **Enhancement Grants**

We greatly appreciate that USDA has turned to the expertise of the microenterprise field in determining whether, and how, to administer an "enhancement grant" portion of RMAP. We strongly believe that RMAP should have a tertiary grant component (separate from TA assistance grants to lenders, and technical assistance-only grants), and have outline our reasoning and recommendations below.

As you know, section 6022(b)(4)(A) of the statute addresses "Grants to Support Rural Microenterprise Development." As stated in the law, these grants are made to MDOs to "provide training, operational support, business planning, and market development assistance, and other related services to rural microentrepreneurs."

First, a plain reading of the statute shows the primary intent to be the provision of core operating grants to MDOs, in order for them to better serve rural microentrepreneurs. Removing examples of the type of technical assistance, the statutory section reads (with the critical words underlined): “The Secretary shall make grants to microenterprise development organizations to (I) provide training ... to rural microentrepreneurs ...”

In addition, report language accompanying the statute provides further guidance in stating that “The Secretary may make a grant under the program to a qualified organization (i) to provide training, operational support, or a rural capacity building service to a qualified organization to assist the qualified organization in developing microenterprise training, technical assistance... and other related services...”

Thus, CFED believes that any “enhancement grant” proposed by USDA should result in both (a) core operating funds for technical assistance providers, and (b) broader field-wide capacity building as further outlined in the report language. CFED strongly believes that this approach structures RMAP in a way that helps to fill the gaps in service that exist in many rural areas.

CFED proposes deleting the “Enhancement Grant” program as suggested by USDA in the Proposed Rule, and replacing it with a “Rural Microenterprise Field Technical Assistance Grant” that adheres to both statute and report language. This grant should have two tracks for which an MDO can apply: (a) providing MDOs with core funding to operate their technical assistance programs, and (b) providing a microenterprise collaborative (e.g. State Microenterprise Association, etc.) with funding for large-scale, field-wide capacity building.

To achieve maximum reach, CFED recommends that all MDOs be permitted to participate in the “Rural Microenterprise Field Technical Assistance Grant” whether or not they already participate in RMAP.

In addition, CFED also proposes that core operating grants be given a funding imperative, with funding provided under the “Rural Microenterprise Field Technical Assistance Grant” split on a 4:1 ratio towards providing MDOs with core funding.

The definition of “significant outmigration” is connected to the concept of Enhancement Grants and the sections of the law under which it would be governed. As such, the Interim Final Rule also deferred a definition of “significant outmigration.” We repeat the comments we made for the Proposed Rule in this regard. The definition of “significant outmigration” should employ definitions of the term (or a similar term) that already exists in law or proposed in legislation. Section 223 of the “American Jobs Creation Act of 2004” (P.L. 108-352, 118 Stat. 1418) defines “high migration rural county” for purposes of eligibility for New

Market Tax Credit investments. For this purpose, “high migration rural county” is defined as any county that has experienced net out-migration of inhabitants from the county of at least 10% during a 20-year period ending with the year in which the most recent census was conducted.

Section 101(3) of the “New Homestead Act of 2007” (S. 1093 as well as the “New Homestead Act of 2006,” H.R. 5380; the “New Homestead Act of 2005,” S. 675; and the “New Homestead Act of 2003,” S. 602 and H.R. 2194) employees a similar definition of “qualifying county” for eligibility of the various provisions proposed in that legislation – a county outside a metropolitan statistical area (defined as such by the Office of Management and Budget) experiencing in a 20-year period a net out-migration of inhabitants from the county of at least 10% of the population of the county.

Lastly, should the Agency implement this recommendation, it will need to develop a separate application scoring process designed to gather and evaluate information on the applicant’s capacity to provide such services and/or their proposed plan for doing so. We recommend that the Agency allow for a public comment period on any new portion of RMAP.

We appreciate the opportunity to comment on the Interim Rule, and greatly look forward to being a resource for USDA as we approach the publication of a Final Rule.

Sincerely,

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