Boston Community Capital
Equity Equivalent Product Description

This memo describes the equity equivalent (EQ2) product and how Boston Community Capital has used it to assist in the capitalization of its affiliates. The equity equivalent was created by the Opportunity Finance Network (formerly National Community Capital Association), Citibank and the Comptroller of the Currency (OCC) as a new form of equity for non-profit community development financial institutions (CDFIs). The OCC has issued an opinion letter approving the EQ2s on behalf of the other federal banking regulators. The Massachusetts Commissioner of Banks has also issued an opinion approving the EQ2s for state chartered banks. After the OFN and Citibank transaction, Boston Community Capital was the first local CDFI in the country to sell EQ2s.

BCC has sold over $10,000,000 in equity equivalents. Bank of America, TD Banknorth, Boston Private Bank, Eastern Bank, Bank of New York Mellon, Belmont Savings Bank, Citizens Bank, Dedham Institution for Savings, Fidelity Management Trust Company, Hyde Park Savings Bank, Investors Bank & Trust, Salem Five Cents Savings Bank, State Street Bank, and Wainwright Bank have all purchased EQ2s from Boston Community Capital. Harvard University, the F.B. Heron Foundation, and the Community Development Financial Institutions Fund (CDFI Fund) of the US Department of the Treasury have also purchased EQ2s from BCLF.

The EQ2 is highly subordinate, below market debt issued for an indeterminate term by non-profit CDFIs. EQ2s support CDFIs in two ways. First, the funds are available to be lent and invested in community development projects. Second, by their subordinated nature, EQ2s leverage additional senior debt from other investors. Banks that purchase EQ2s are allowed to receive CRA credit for a proportionate share of the CDFI's entire lending activity that greatly enhances the CRA credit of the investment. In addition, banks may claim favorable accounting treatment for the EQ2. Boston Community Capital (BCC), through its subsidiary Boston Community Loan Fund (BCLF), is selling EQ2 to assist in the capitalization of the BCLF.

Required Attributes of the EQ2

To qualify as an EQ2, the investment must have the following characteristics:

- be a general, unsecured obligation of a non-profit CDFI;
- be fully subordinated to the right of repayment of all other creditors of the CDFI;
- payments cannot be accelerated;
- any interest rate must not be tied to the income of the CDFI;
- have an indeterminate term. An initial ten-year "tenor" that annually will be rolled back to a new ten-year tenor meets this test;
- cannot be an ordinary loan or debt instrument of the CDFI;
- for banks, the CDFI must make loans or investments that benefit the bank's CRA assessment area or a broader statewide or regional area that includes the assessment area.

CRA treatment

Banks that purchase equity equivalents receive CRA credit for a *pro rata* share of all the CDFI's lending during the life of the EQ2. The *pro rata* share is calculated by the value of the EQ2 divided by the total equity capital of the CDFI. For example, if a bank purchased an EQ2 for $1,000,000 that resulted in the CDFI having total equity capital of $4 million, the bank's pro rata share would be 25%. With an equity base of $4 million, the CDFI would expect to have total capital of $30 million. Assuming (very conservatively) a $10 million level of lending over the next 10 years, the CDFI would do $100 million in lending and the bank would receive CRA credit for 25% of the total, or $25 million. The bank can choose to take the CRA credit under either the lending or investment test. In Boston Community Capital's specific case, our first equity equivalent investors purchased EQ2s in August 1997 and, in the first year, received pro rata CRA credit of 3.7 times their initial investment. Through the end of 2009, those investors have received CRA credit more than 20 times their investment.

Accounting Treatment and Permissibility

Banks purchasing EQ2s can carry them on their balance sheets as "other assets." Therefore banks can avoid loan loss reserve requirements. Banks may be able to value the EQ2 at cost and discount the below market interest on an annual basis (rather than when booking the EQ2). EQ2s are considered "qualified investments" under 12 CFR 25, 228, 345, and 563 as determined by the Office of the Comptroller of the Currency, Community and Consumer Law Division.

Boston Community Capital

The terms of the equity equivalents created by Boston Community Capital meet the regulatory requirements for EQ2s. They are issued by BCC's subsidiary Boston Community Loan Fund (BCLF). The BCLF's purposes are to provide direct loans to community based projects and to capitalize affiliated community based financial intermediaries.

The terms of the BCLF's equity equivalents include:

interest rate:	Up to 3% paid annually
term:	10 year minimum initial term extended annually. During first five years EQ2 is rolled automatically if performance covenants are met.
subordination:	subordinate to all other creditors of BCLF.
limited recourse:	BCLF shall not be required to repay if any or all of such repayment should put the BCLF out of compliance with any senior creditors, including violation of permanent capital and liquidity requirements (or any such comparable requirements which may exist at the time of maturity.)
documentation:	a standard loan agreement and note will be executed for the investment.

For more information

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