Native CDFIs: Strengthening the Fabric of Rural America

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Introduction

Rural America is a diverse patchwork of communities composed of Black, Latinx, Appalachian, Native American, white and other populations. Their homes, cultures, languages, businesses, and even the foods they eat may look different, but their economies share an unfortunate commonality: Remoteness, historic disinvestment and systemic racism have impeded economic growth in each of these places.

A more welcome common thread that ties these communities together is a network of committed organizations called community development financial institutions, or CDFIs. These entities discover budding entrepreneurs, promising businesses and aspiring homeowners, and launch them on their journeys toward self-sufficiency and economic success in ways that help to mend the rips and tears of history.

Some of the deepest slashes in the fabric of rural America have been in Native communities. Thirty-five states are home to American Indian, Alaska Native and Native Hawaiian people, and CDFIs have played a critical role in supporting them. Many carry a special designation as "Native CDFI," a U.S. Department of the Treasury charter specifically for institutions with at least 50% of their activities in Native communities.

By examining how members of the Oglala Sioux Tribe on the Pine Ridge Indian Reservation in South Dakota have been impacted by the work of three Native CDFIs, this chapter explores how these institutions are uniquely positioned to deliver customized financial products and services that advance economic viability in underserved Native communities and reverse the trends of historic disinvestment. The chapter also shares four key takeaways that would help to expand the impact of Native CDFIs.

Understanding the Federal Trust Responsibility to Indian Tribes

History has not been kind to many rural populations in America, especially to Native Americans. The federal policies of genocide, colonization and relocation are not widely discussed in classrooms, where lessons about Indigenous people are more likely to cover Thanksgiving folklore. To understand the economic development landscape for tribes, a more realistic and relevant history lesson is necessary.

In the 1800s, the United States, in a series of three Supreme Court decisions known as the "Marshall Trilogy," recognized the sovereignty of Indian tribes and their right to self-govern, and established a "guardian-ward relationship" between the federal government and tribes.[1] This fiduciary duty, along with the 370 mostly unfulfilled treaties entered with tribes throughout the 19th century, resulted in a trust responsibility between the federal government and tribes. This is a key doctrine that has had many far-reaching implications for the economic conditions in Native communities.

In its simplest form, the federal trust responsibility means that because the federal government took Indian land, it has a responsibility to protect and provide for Indian people. This federal policy is what sets Native people apart from other U.S. citizens when it comes to federal programs. Federal resources allocated for the benefit of Indian tribes and their members are not based solely on need or any of the other typical indicators of government interventions. They fulfill a federal trust responsibility.

The federal government's trust responsibility to tribes also affects the land status of Indian reservations. Most land within the boundaries of a reservation is held in trust for the benefit of an Indian tribe or an individual Native American. This policy has protected Indian land from leaving tribal control, but it has also made doing business in Native communities different than in other rural communities, sometimes requiring complicated and lengthy approval processes to use land as collateral for financial transactions.

Despite the systemic challenges created by American history and these federal policies, Indigenous communities have persevered and prospered.

An Introduction to CDFIs

CDFIs are financial entities that focus on the economic health of the markets they serve by providing access to financial products and services for community members and businesses. A CDFI can be a bank, a credit union or a loan fund, but what distinguishes these lenders from traditional profit-driven banks is their community development mission that complements a desire for generating revenue to achieve organizational sustainability.

What does that mean in practice? CDFIs develop deeper relationships with their clients and have more flexibility to design loan products suited to their clients' financial situations, which might include lower incomes, fewer assets, and limited or poor credit histories. This approach to lending has been successful in times of both economic crisis and growth.

According to the Opportunity Finance Network (OFN), a national network of CDFIs, as of February 2021, more than 1,200 CDFIs are certified by the U.S. Department of the Treasury's CDFI Fund, with about $222 billion in assets. OFN reports that from 1999 to 2017, CDFIs outperformed insured depository institutions with lower loan-loss rates. This track record is a true indication of the effectiveness of local, community-based connections and the credit worthiness of these often-overlooked communities.

Native CDFIs

When Congress created the CDFI Fund in 1994, several tribes and Native organizations advocated for a set-aside specifically for Native communities. At the time, policymakers were reluctant to carve out dedicated funding for one population over another, so they directed the CDFI Fund to conduct a study about the capital and credit needs of American Indian, Alaska Native and Native Hawaiian people. The resulting 2001 Native American Lending Study identified 17 major barriers to capital access, relating to legal infrastructure; government operations; economic, financial and physical infrastructure; and educational and cultural issues.

This recognition of the challenges associated with accessing credit in Native communities, combined with the federal government's trust responsibility to Indian tribes and the political status of Indigenous people, led to the creation of the CDFI Fund's Native American Initiative, which included a separate charter for CDFIs serving Native populations, as well as a dedicated funding stream.

When the initiative started in 2003, there were only 14 Native CDFIs certified by the CDFI Fund. As of June 2021, there were 69 and nearly as many emerging entities. These organizations collaborate with other stakeholders in their target markets to build the financial capability of their clients and prepare them to access affordable consumer loans, microfinancing, mortgages, small-business startup loans, agriculture loans and other commercial financing. A recent study indicates that communities with Native CDFIs show significant increases in credit scores compared to communities with only non-Native CDFIs.[2]

Native CDFIs also serve as an impetus in their communities to break down many of the barriers identified in the 2001 study, e.g., prompting the enactment and refinement of tribal codes that provide legal remedies in their tribal jurisdictions, the development of physical infrastructure, and the recruitment of private-sector providers, including appraisers, contractors and insurance providers.

Native CDFIs on the Pine Ridge Indian Reservation

Like many rural places, the Pine Ridge Indian Reservation faces the hardships of remoteness. It is nestled in the prairies of the Great Plains and spans 2.1 million acres, more than twice the size of Rhode Island. The reservation is home to 20,000 enrolled members of the Oglala Sioux Tribe, one of nine tribes located in the state of South Dakota. Nearly 40% of families live below the poverty level, and unemployment rates can soar up to 80%. There are few businesses or even places to buy food on the reservation, so tribal members must travel to border towns to purchase necessities.

Housing stock is limited, and much of what exists is in poor condition and in need of repair. Overcrowding is a constant challenge, with multiple generations residing under one roof. Physical infrastructure, including roads, water and sewer, electrical utilities and broadband, are not adequate to support the expanding local economy that the community desires.

Amid these harsh conditions, prosperity is emerging. Thanks to the quiet work of a small group of community development practitioners, tribal members have turned to CDFIs as trusted advisers who understand their circumstances and can help them achieve their dreams for the future. Over the past four decades, three Native CDFIs have contributed to the economic growth of the tribal members of the Oglala Sioux Tribe through business, mortgage and consumer lending.

Lakota Funds

Some of the earliest development efforts began in the late 1980s, when a group of organizers gathered to explore strategies to seed local businesses on the reservation. At the time, there were no tribal member-owned businesses, and 75% of the respondents to a community survey had never had a loan or even a checking or savings account. The organizers knew this would be a high-risk market, but they also knew they had to start somewhere. Thus, they established Lakota Funds in 1986.

Hindsight has revealed many mistakes to the organizers. Their funders were pressuring them to deploy capital quickly, and they did so before borrowers were ready to take on this financial responsibility. One of the most important lessons learned was the realization that expanding personal financial capacity was a critical first step to ensuring the success of business development. Also, in a community reliant on public assistance and grants, building a relationship with new borrowers to create an expectation of repayment was key, and strengthening collection efforts was a dreaded but necessary undertaking. Another part of Lakota Funds' financial education program was helping borrowers to understand that repaying their loans made it possible for the organization to relend that capital to other businesses.

Over the years, the borrowers and their businesses matured. One of Lakota Funds' first clients was Dale McGaa, who acquired a loan for a belly dump trailer in 1986 and went on to operate Crazy Horse Construction as a successful contractor in business for more than 30 years before he retired. Lakota Funds' founders attribute much of the impact they had on the reservation to their focus on lending to construction companies owned by tribal members who supported economic growth in the community.

Lakota Funds matured along with its market. After a period of experimentation, Lakota Funds incorporated in 1993 and was certified by the CDFI Fund as a Native CDFI in 2000. Along with its business loans, it began offering extensive services designed to expand financial capability, including credit coaching, matched savings accounts and basic financial skills courses. Today, Lakota Funds is still designing business loans to meet the unique demand from its market, most recently adding agriculture loans for Native ranchers to its list of loan products.

By remaining close to the community, Lakota Funds has tailored its loan underwriting criteria to its market risk—something that is harder for banks to do. Lakota Funds' knowledge and experience in its target market helped its loan committee to understand that the usual predictors of repayment don't apply here. For example, low credit scores and income levels have not resulted in poor loan performance, but the length of a borrower's employment in a job, no matter the type of job, makes a difference. This understanding of the market risk has helped Lakota Funds to become a successful and profitable lender in a market considered by others to be too risky.

As of December 2020, Lakota Funds had loaned more than $16.3 million through 1,225 total loans, aiding 823 businesses and creating over 2,000 jobs—an impressive contribution to the economy of the Pine Ridge Indian Reservation and the surrounding communities.

Mazaska Owecaso Otipi Financial

As tribal members began to accumulate more assets in the early 2000s, another movement began. The Oglala Sioux Tribe Partnership for Housing, a new housing nonprofit, began seeking potential lending partners to meet the rising demand for homeownership on the reservation. In 2004, it helped to launch a second Native CDFI serving the reservation. Mazaska Owecaso Otipi Financial set out with a mission to create safe and affordable housing opportunities on the Pine Ridge Indian Reservation by providing loans, training and financial insight to empower Native people to build assets and create wealth.

Mazaska partnered with other mortgage lenders but also began designing its own portfolio loan products, customized to the distinct needs of its borrowers. Its mortgage products offer flexible underwriting criteria and accept a leasehold interest in the land, rather than the land itself, as collateral. In addition to providing intensive financial and homebuyer education, Mazaska provides technical assistance to help its clients obtain all the necessary tribal and federal clearances for encumbering trust land with a mortgage—a complicated process with many steps that has the potential to delay the transaction.

The Native CDFI also developed a credit-builder loan to help prospective homebuyers improve their credit worthiness before qualifying for mortgage financing. In addition, it provides a range of down payment assistance options to help make homeownership more affordable for its clients.

Nearly 17 years later, Mazaska is still a key financing partner on the reservation, collaborating frequently with Lakota Funds to serve their mutual clients. Clients in need of improving basic financial management skills may attend Lakota Funds' courses first and then start working with Mazaska on the homebuying process. The two CDFIs have also worked together to offer participation loans. For example, one borrower whose business location included residential space accessed a joint loan, with Mazaska providing the mortgage financing and Lakota Funds financing the business purchase.

The two Native CDFIs also share a commitment to serving Native veterans in their community. Lakota Funds provides technical assistance to help veterans prepare for the homeownership process and offers a matched savings account designed specifically for veterans. Mazaska provides loan packaging services for the U.S. Department of Veterans Affairs' Native American Direct Loan program, as well as other financing services.

Lakota Federal Credit Union

In January 2009, community organizers once again gathered to discuss options for bringing a depository institution onto the Pine Ridge Indian Reservation. Lakota Funds anxiously agreed to sponsor the proposed Lakota Federal Credit Union. A steering committee began the nearly three-year process of establishing the first and only federally insured financial institution on the reservation.

In August 2012, the Lakota Federal Credit Union received its charter from the National Credit Union Administration. Located in the Lakota Trade Center in Kyle, South Dakota, it offers savings accounts, checking accounts, check cashing, direct deposit and consumer loans, both secured and unsecured, to members who live, work, worship, attend school or volunteer on the Pine Ridge Indian Reservation. In 2013, the CDFI Fund certified the credit union as a Native CDFI.

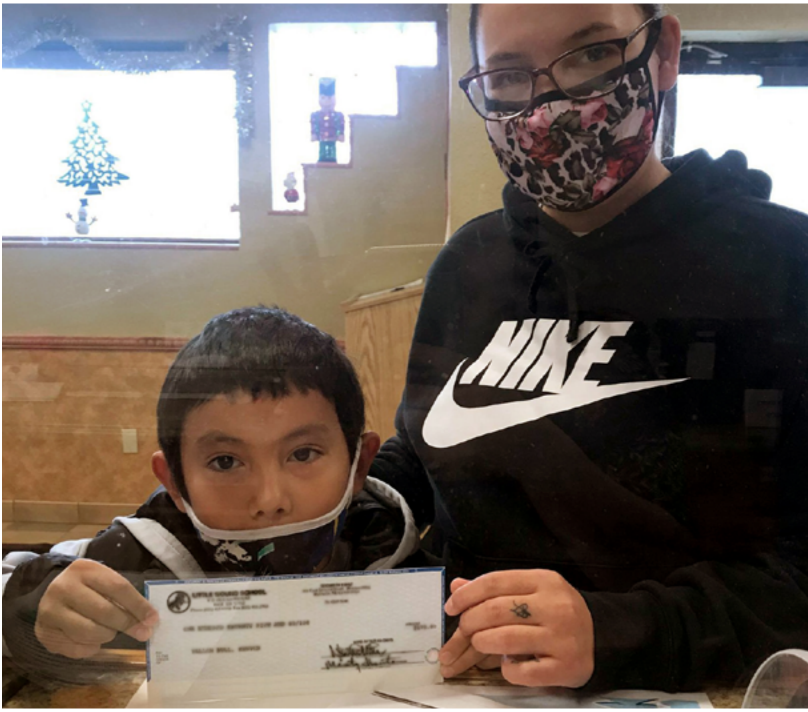
Before the Lakota Federal Credit Union started providing financial services, the reservation population was 60% unbanked. Now all community members have access to basic savings accounts to plan for their financial futures. Since opening its doors in September 2012, the Lakota Federal Credit Union has accumulated $7.1 million in assets, attracted 3,000 members and deployed 450 loans, for a total of $2.4 million. The credit union's rapid growth is attributed to the fact that all of its employees are tribal members who can relate to the financial needs of their customer base.

In a community where hopelessness and poor economic and health conditions have fueled high suicide rates and limited length of life, Lakota

A young Lakota Federal Credit Union member making a deposit into her account. Source: Lakota Federal Credit Union.

Federal Credit Union sees itself playing an important role in the community's vibrancy. The credit union is helping its members to have a sense of hope for their futures while providing financial tools to help them get there. One of its brightest beacons of light is seeing young children visit the credit union with their parents or grandparents to make deposits into their savings accounts. This young generation of savers is poised to bring about even bigger economic impacts to the community going forward.

In their own ways, Lakota Funds, Mazaska and Lakota Federal Credit Union have each proven they have the expertise to operate in persistent poverty areas to support economic, social and racial justice. By providing basic financial management skills and customized loan products, they are preparing their borrowers to overcome systemic barriers to accessing credit by acting as conduits to mainstream financial institutions.



A young Lakota Federal Credit Union member making a deposit into his account. Source: Lakota Federal Credit Union.

Key Takeaways

This historical review of the Native CDFIs serving the Pine Ridge Indian Reservation reveals four key takeaways that could help expand their impact and the impact of similar Native organizations across rural America:

1. **Native CDFIs are ripe for private-sector investment.** Private-sector funders, including foundations and individual donors, should invest directly into established Native CDFIs with a proven track record of meeting the financing needs of their communities while achieving organizational sustainability. Possible investments could include low-cost, long-term loans or grants to support lending and operating capital. In addition, funders interested in building the capacity of startup Native CDFIs could invest in regional or national intermediary organizations that support emerging entities.

2. **Collaborations between mainstream financial institutions and Native CDFIs offer market expansion and systemic change opportunities.** Native CDFIs are valuable partners for mainstream financial institutions exploring market opportunities in underestimated Native communities. Therefore, lenders seeking to expand their products and services with an eye toward achieving both growth and racial equity should explore opportunities to collaborate with Native CDFIs.

3. **Positive Community Reinvestment Act (CRA) consideration could provide additional incentives for regulated financial institutions to partner with Native CDFIs.** Federal banking regulators could increase the likelihood of regulated entities' engaging in lending and investment activities with Native CDFIs by giving them credit for such activities under their CRA obligations, even if the CDFI loan recipients are not located in the lenders' assessment areas.

4. **The federal government should allocate more resources to Native CDFIs.** Native CDFIs have proven themselves to be good stewards of federal resources, yet substantial needs remain in the Native communities they serve. Allocating federal dollars to Native CDFIs would reverse the historic trend of disinvestment in areas of high need and persistent poverty, and would provide an effective mechanism for the federal government to fulfill its trust responsibility to Native nations. Specifically, Congress should increase appropriations to the CDFI Fund's Native American Initiative and expand the use of Native set-asides for federal programs that stimulate economic development, like the New Markets Tax Credit program. Congress should also identify opportunities to improve the deployment of federal direct loans—for example, the U.S. Department of Agriculture's Single Family Housing (Section 502) Direct Home Loan and U.S. Department of Veterans Affairs' Native American Direct Loan—by allowing Native CDFIs to serve as intermediary lenders to relend to eligible borrowers in Native communities.

Increased engagement from private-sector funders, mainstream financial institutions and the federal government can only bolster the promise of Native CDFIs to respond to the historical and economic issues experienced by Native communities. As we have seen on the Pine Ridge Indian

Reservation, Native CDFIs are critical agents of systemic change. As community and industry leaders across the country rise to weave together their strategies of hope and economic resiliency, Native CDFIs will continue to strengthen the fabric of rural America by helping Indigenous populations overcome historical trauma, repair systemic injustice and stimulate economic opportunity.

References

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Wikipedia. "Tribal Sovereignty in the United States." See https://en.wikipedia.org/wiki/Tribal_sovereignty_in_the_United_States#The_Marshall_Trilogy,_1823-1832.

Endnotes

1 "The Marshall Trilogy is a set of three Supreme Court decisions in the early nineteenth century affirming the legal and political standing of Indian nations: Johnson v. M'Intosh (1823), holding that private citizens could not purchase lands from Native Americans; Cherokee Nation v. Georgia (1831), holding the Cherokee nation dependent, with a relationship to the United States like that of a 'ward to its guardian'; and Worcester v. Georgia (1832), which laid out the relationship between tribes and the state and federal governments, stating that the federal government was the sole authority to deal with Indian nations." (See Wikipedia.)

2 See Kokodoko et al.