

## Changes to CRA Regulation by Treasury on the Horizon



Treasury Secretary Steve Mnuchin said, "I want to make sure <CRA> is absolutely going to help communities and isn't just a 'check the box' to satisfy regulators." Above, Mnuchin being sworn in at the Oval Office.

The banking community is anxiously awaiting the announcement from the Treasury Department with its proposed revisions to Community Reinvestment Act ("CRA") regulations. While some constituents are hopeful that the revisions will modernize regulations and make the law less bureaucratic, others are concerned that any rollback could mean low-income borrowers over time will have less access to loans and banking services. Treasury has indicated that it is planning on unveiling its recommendations in early 2018. It is yet unclear as to what Treasury will propose (Continued on page 3)

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## SBA Loan Fund Receives Highest Possible Credit Rating from Moody's Investor Services

On January 10, 2018, Solomon Hess Capital Management ("Solomon Hess") announced that its flagship CRA-eligible SBA Loan Fund received the highest possible credit rating from Moody's Investor Services. This Aaa-bf bond fund rating is based on Moody's assessment of the creditworthiness of the portfolio and is an indication that the SBA Loan Fund holds assets judged to be of highest credit quality. Managing Director of Solomon Hess Bill Einstein said, "The SBA Loan Fund received the highest possible rating given by Moody's (triple A), which reflects the portfolio's composition of such a high concentration of directly federally guaranteed assets."

The SBA Loan Fund is a certified Community Development Entity that primarily invests in the debt of small businesses located in lower income communities targeted by investors. In 2017, the SBA Loan Fund invested

roughly \$270 million in 423 small businesses loans nationwide. The SBA Loan Fund had \$487 million in assets as of December 31, 2017 and added its 112th bank investor, reinforcing its acceptance as a CRA-eligible investment fund for banks seeking community development credit. The 882 small business loans currently in the portfolio supported the creation and/or retention of 14,941 jobs, 87% of which are located in lower income communities.

*"The Moody's rating reinforces the SBA Loan Fund's position in the marketplace as a CRA community development investment fund that offers high quality targeted impact with high credit quality assets," Einstein said.*

Since inception in 2004, the SBA Loan Fund has invested \$1.5 billion in over 3,000 small business loans which supported over 41,000 jobs nationwide. ■

## SBA Loan Fund Profile: Piedmont Piano Company in Alameda, California

An example of the type of loan in the SBA Loan Fund portfolio is the loan to the Piedmont Piano Company, a family owned business that sells top quality pianos in a low income census tract in Oakland, CA. The company is a factory authorized representative for a wide range of pianos and specializes in selling fine used pianos. Piedmont Piano Company offers quality piano rentals both long and short term and also operates a music school that provides classes and lessons for all ages.

The Callahan family founded the company out of a rented garage on Piedmont Avenue in 1978. From the beginning, they (Continued on page 2)



The Piedmont Piano Company was founded by the Callaban family in 1978 as a family owned and operated business that specializes in refurbishing used pianos. Founder Jim Callaban Sr. learned the trade of piano tuning to supplement his income as a musician (French Horn section) with the San Francisco Symphony. Jim established The Piedmont Piano Company with his three sons Jim Jr., John and Michael. Above, a Steinway grand piano.

**Small Business Profile: Piedmont Piano Company** (from page 1) focused on refurbishing used pianos into long lasting instruments for customers. They specialized in vintage Steinways. In 1980, they moved into their first storefront location at 6260 Piedmont Ave. In 1984, the Callahans acquired Mills Music and became a factory authorized dealer for Yamaha acoustic and digital pianos. Carrying new pianos necessitated a move to a larger facility and, in 1985, the store relocated to 4238 Piedmont Ave. Included in the assets of Mills Music was the Yamaha Music School, now the Harmony Road Music School, which has taught music to many students.

As business grew, a second location on Third Street in San Francisco was opened in 2004. However, a dramatic rent increase and troubled economy forced the Callahans to close this location only four years later. As they looked for a new location, they were thrilled to find the current location in Oakland's developing Uptown Arts & Entertainment district and were able to finance the purchase of the building in 2009 after a long negotiation and a SBA 7(a) loan. The current storefront opened in January 2010 and has since done very well.

The Piedmont Piano Company applied for a second SBA 7(a) loan in September 2017 to finance the purchase of equipment. This loan qualifies for CRA as the business is located in a low income census tract and a CDFI Fund Qualified Investment census tract. The borrower self-reported that this loan supported the creation/retention of 7 jobs. This loan is one example of the types of loans in the SBA Loan Fund portfolio. ■

**Did you know?** Loans made to a recently formed small business that promotes economic development qualifies for CRA under community development. The most recent set of CRA Q&A published in July 2016 expanded the list of activities to promote economic development if they supported permanent job creation/retention/improvement to include financing intermediaries that lend to, invest in, or provide technical assistance to start-ups or recently formed small businesses or farms<sup>1</sup>.

## Tax Overhaul Results in Lowering of LIHTC Valuations

Last spring CRAnews reported that the mere possibility of cut backs in the tax credit program had cast a shadow over the Low Income Tax Credit ("LIHTC") program, which promotes investments in affordable housing and is the cornerstone of many banks' CRA investments. At the time, the market was seeing tax credit valuations 10-20% lower since Election Day in anticipation of tax cuts. Approved last month, the tax plan has resulted in a further decline of tax credit values in the market today. According to analysis by Novogradac & Company, a national accounting firm, the new tax law will reduce the growth of subsidized affordable housing by 235,000 units over the next decade, compounding an existing shortage. ■



The LIHTC program is widely regarded as being a successful and popular program. Unlike public housing programs, LIHTC has proved enduring and politically popular. Since 1987, tax credits have funded construction and rehabilitation of about 30% of the nation's 10 million affordable housing units, which are defined as units that people making 60% or less of a city's median income could afford. Above, a construction site.

## SBA Loan Fund Raises Preferred Return Again

The SBA Loan Fund raised its Preferred Return for Q1 2018, marking the six increase since Q1 2016. The Preferred Return is re-set each quarter and is annualized and net of all expenses and fees (including management fee). For Q1 2018, the Preferred Return is set at 2.35% for targeted CRA investments and 2.45% for non-targeted CRA investments. This increase in the Preferred Return demonstrates the continued strong performance of the SBA Loan Fund's assets in a rising interest rate environment.

## SBA Loan Fund Profile: Jefferson Crest in Milwaukee, Wisconsin

Another example of a type of loan in the SBA Loan Fund portfolio is the loan to Jefferson Crest in Milwaukee. Jefferson Crest provides a state-licensing Community Based Residential Facility to accept ambulatory clients who are mentally ill, developmentally disabled and elderly. The company also provides living accommodations in supported living apartments and in-home assistance personal care services. Services include independent shared environment, 24-hour personal care assistance, on call RN and feeding assistance. Jefferson Crest is a minority owned and operated business that manages 12 locations. Jefferson Crest applied for a SBA 7(a) loan to finance the purchase of equipment.



Jefferson Crest is a minority owned and operated business that provides quality skilled care to persons who are elderly, developmentally disabled or mentally ill. Above, a nurse providing care.

This loan qualifies for CRA as it is located in a low income census tract. The borrower self-reported that this loan supported the creation/retention of 100 jobs. ■

<sup>1</sup>Q&A\_\_12(g)(3)-1.

**Changes to CRA Regulation** (from page 1) as changes to the CRA but thus far the banking community seems to be supportive of the review process.

**Origins of the CRA** The CRA was enacted in 1977 to ensure that banks serve the needs of the communities they are in and to specifically ensure that low income borrowers have access to the financial system. The law has become a contentious topic of late as advocates want to see its protections strengthened while opponents argue that regulations haven't kept up with changes in technology, don't recognize some forms of lending and penalize activities that aren't directly tied to CRA.

**Treasury Assessment** When Treasury initiated its review of CRA in June 2017, it was with the goal of assessing how the CRA framework could be reformed and modernized, including by (1) improving how banks' CRA investments are measured to improve benefit to communities, (2) harmonizing CRA-related oversight, (3) changing the way CRA geographic assessment areas are defined in light of technological and other factors, and (4) improving the regulatory review and rating assessment process. The objective of the review was not to advocate the repeal of the CRA but to propose changes to make the CRA more transparent and consistent.

**At a congressional hearing last June, Treasury Secretary Steve Mnuchin said, "Banks spend billions and billions of dollars fulfilling CRA obligations. I want to make sure it is absolutely going to help communities and isn't just a 'check the box' to satisfy regulators."**

As part of its review process, Treasury solicited input from key stakeholders and has plans to work with all three regulators in development recommendations.

**Definition of Community Development Under Review** One major component under review is the reporting of measures targeting low or moderate income individuals ("LMI") in areas where a bank

operates. Comptroller of the Currency Joseph Otting has suggested expanding the activities to include small business loans. The Bankers Association ("ABA") goes even further to suggest that infrastructure lending and activities that don't solely benefit LMI also be included. The ABA argues that banks would have more flexibility to do more to help communities, such as by revitalizing rural areas. On the other side, the National Community Reinvestment Act Coalition ("NCRC"), a fair-lending advocacy group, argues that expanding the definition of community development would reduce the services available to the poor and inflate banks' CRA ratings. Essentially, the NCRC claims that there would be less spending on services that specifically benefit LMI.

***"If you begin to move away from the focus on income and class of the borrower and begin to expand it <community development>, you're really changing the law," said John Taylor, president of the NCRC.***

**Rating Assessment and Penalties Under Review** Also under review is the complex rating assessment process and penalties for compliance issues. Bankers have long been calling for more transparent and consistent scoring rubrics and more timely performance results. Some banks have also called for limiting CRA rating grades to reflect only CRA related lending activity. In the past, some banks' CRA grades were downgraded for a wide range of alleged misconduct. For example, Wells Fargo, Fifth Third Bancorp and Regions Bank had their CRA performance ratings downgraded due in large part to settlements involving other laws. Movement towards making it harder for banks to be downgraded for reasons not directly tied to CRA lending has already been made by the Office of the Comptroller of the Currency ("OCC"). In October, the OCC changed its CRA supervision policies to make downgrades of banks' CRA rating supported by instances of discriminatory or illegal credit practices directly related to CRA lending activities. ■

## Reaction from Banking Community

***At the CRA & Fair Lending Colloquium held in November 2017, there was a general consensus that a modernization of the CRA is imperative to ensure the efficacy of the spirit of the law and the relevance of CRA going forward. There was wide support for the process by which Treasury was conducting its review and affirmation that Treasury had met with over 60 CRA stakeholders including bankers and advocacy groups and that the meetings were positive in nature. At the time, the Agencies had yet to meet with Treasury but representatives from all three regulators were looking forward to collaborating on revisions to CRA.***

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[www.piedmontpiano.com](http://www.piedmontpiano.com)

[www.jeffersoncrest.com](http://www.jeffersoncrest.com)

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*We will be exhibiting at the  
National Interagency  
Community Reinvestment  
Conference in March!*

## 2018 Conference Calendar

National Interagency Community  
Reinvestment Conference

March 18 –21, Miami, FL

CRA & Fair Lending Colloquium

November 4-7, Hollywood, FL

[www.cracolloquium.com](http://www.cracolloquium.com)

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## Managing Good Capital Well

Solomon Hess Capital Management (“Solomon Hess”) is an alternative asset manager specializing in fixed income. Our mission is to provide investors with community and economic development-focused investment funds that generate both competitive risk-adjusted returns and positive quantifiable community impact. Founded in 2004 and located in Falls Church, Virginia, Solomon Hess has over \$600 million of assets under management. Solomon Hess is Fund Manager to the SBA Loan Fund and investors include banking institutions of all sizes that are seeking Community Development Investment or Lending test credit within the Community Reinvestment Act (CRA) rules via exposure to SBA 7 (a) loans and related assets. Other investment opportunities with Solomon Hess include investing in our Absolute Return strategy fund or our Community Impact Fund (under development).

*The Solomon Hess SBA Loan Fund LLC attempts to provide its investors with CRA credit related to their participation in the Fund. Investment decisions are not always exclusively based on the economic characteristics or investment merit of a specific asset. Certain CRA eligible securities sought by the Fund in specific geographies may not provide as great an economic benefit to the Fund as the same securities located in non-CRA geographies. The Fund may engage in transactions at times for reasons related to CRA considerations that may not be desirable from an investment standpoint. If one or multiple federal banking regulators, such as the OCC, FDIC or the Federal Reserve Board, were to deem an investment in the Fund as not qualifying for CRA credit, the impact to Fund investors could be material.*