August 5, 2022

BY ELECTRONIC TRANSMISSION

Chief Counsel’s Office
ATTN: Comment Processing
Office of the Comptroller of the Currency
400 7th Street, S.W., Suite 3E-218
Washington, D.C. 20219

Ann E. Misback, Secretary
Board of Governors of the Federal Reserve System
20th St., and Constitution Ave., N.W.
Washington, D.C. 20551

James P. Sheesley, Assistant Executive Secretary
Federal Deposit Insurance Corporation
550 17th Street, N.W. Washington, D.C. 20429

RE: Community Reinvestment Act, RIN 3064-AF81, Docket ID OCC-2022-0002

On behalf of its membership, the Small Business Investor Alliance (“SBIA”) is pleased to submit the following comments in response to the above-referenced joint notice of proposed rulemaking (“Proposal” or “CRA Rulemaking”) by the Office of the Comptroller of the Currency (“OCC”), Board of Governors of the Federal Reserve System (“Board”), and the Federal Deposit Insurance Corporation (“FDIC”), and together the “Regulators,” regarding modernizing the Community Reinvestment Act of 1977 (“CRA” or “Act”) regulatory and supervisory framework.\(^1\)

The SBIA is the national organization that represents small business funds and their investors, including Small Business Investment Companies (“SBICs”), some non-SBIC funds, and the many banks that invest in them. These funds make important economic development contributions to job creation, retention, and improvement, including in under-served areas and among under-represented groups, and can provide a valuable vehicle for first-time fund managers, including founders of color and other emerging managers that may focus on early-stage small businesses.

\(^1\) 12 U.S.C. 2901 et seq. The Board implements the CRA through Regulation BB at 12 CFR part 228. The OCC is the primary CRA examiner for national banks and federal savings associations and implements the CRA through 12 CFR part 25. The FDIC has CRA examination authority over certain state-regulated financial institutions and implements the CRA through 12 CFR part 345.
I. Economic Development

a. SBIC and RBIC Investments are Economic Development

Regulators are unambiguous in the proposed rulemaking that bank investments in SBICs and rural business investment companies ("RBICs") will qualify for CRA credit consideration as community development investments fully without limitation because those investments are considered economic development undertaken consistent with the rules governing those particular federal programs.\(^2\) SBIA strongly endorses this alignment.

Specifically, the proposed rule states that bank "lending to, investing in, or providing services to ... SBICs ... or U.S. Department of Agriculture Rural Business Investment Companies would qualify as economic development" (emphasis added).\(^3\) The proposed rulemaking includes unambiguous language that the rules governing the SBIC and RBIC programs would govern when evaluating CRA credit consideration including "using the standards established by ... SBICs for loans, investments, or services" to the small businesses supported through them.\(^4\) While it is implied in the Proposal's text, SBIA urges the Regulators to state expressly that all subcategories of SBICs are covered under this express language (e.g., Specialized SBICs, bank-owned SBICs, and all other subsequent categories).\(^5\)

The proposed rulemaking also stipulates that this prong of the "economic development" definition would leverage the small business size standards applied both by the U.S. Small Business Administration ("SBA"), which is the primary regulator for the SBIC program, and the RBIC program.\(^6\) The Regulators also use unambiguous language to separate from application here the

\(^2\) CRA Rulemaking, 87 Fed. Reg. 33884, 33899 (June 3, 2022). "Economic development" is one of four broad categories of activities comprising community development under which a bank is evaluated for CRA credit. The other three categories are affordable housing, community services, and revitalization and stabilization. CRA Rulemaking at 33891. SBICs, administered by the U.S. Small Business Administration ("SBA"), are highly regulated private funds that invest exclusively in domestic small businesses, which by statutory mission provide capital that is otherwise unavailable or in short supply to small businesses. Small Business Investment Act of 1958, Pub. L. 85-699 (Aug. 21, 1958). 15 U.S.C. 661. Related, the U.S. Department of Agriculture ("USDA") operates the RBIC program, a developmental venture capital program for the purpose of promoting economic development and the creation of wealth and job opportunities in non-metropolitan areas and among residents living in those areas. Like the SBA, the USDA licenses investment fund applicants to address the unmet capital needs of small enterprises primarily located in rural areas. The RBIC program does not offer its licensees federally guaranteed capital access like the SBIC program.

\(^3\) Id.

\(^4\) CRA Rulemaking at 33899.

\(^5\) Section 301(d) of the Small Business Investment Act of 1958 authorized licensing for specialized small business investment companies (SSBICs) that focus on financing small businesses "whose participation in the free enterprise system is hampered because of social or economic disadvantage." PL 92-595, Small Business Investment Act Amendments of 1972. Congress repealed Section 301(d) in 1997, but successful SSBICs were grandfathered and allowed to remain in the program. A "bank-owned SBIC" generally is a commercial bank that under federal regulation may invest up to five percent of their regulatory capital and surplus to partially or wholly own an SBIC.

\(^6\) See 13 CFR part 121. To determine eligibility for federal small business assistance, SBA uses two primary measures of industry-based size standards (13 CFR 121.201) to define "small business": (i) average annual receipts, and (ii) average number of employees. The SBIC program, moreover, may use either the industry-based size standards or tangible net worth (<$19.5 million/ including affiliates) and average net income
gross annual revenue threshold of $5 million or less applied under the proposed Retail Lending Test and elsewhere in the proposed rulemaking to define "small business".\(^7\)

We commend the Regulators for making this clear distinction and encourage them in the final rulemaking to emphasize again explicitly that bank investors in SBICs and RBICs will receive CRA credit for all eligible investments made by the fund, and not just for certain investments in, for instance, "smaller enterprises" because a statutory purpose of these programs includes helping expand capital access to all small businesses.\(^8\)

\(\textit{b. Economic Development also Includes Non-SBIC Financial Intermediaries Whose Investments Create Jobs}\)

SBIA applauds the Regulators for recognizing within the proposed definition of "economic development" activity that non-SBIC financial intermediaries also invest in small businesses because CRA credit eligibility includes "support for financial intermediaries that lend to, \textit{invest in,} or provide technical assistance to businesses or farms with gross annual revenues of $5 million or less" (\textit{emphasis added}).\(^9\)

SBIA suggests that the Regulators provide more clarity here by adding that the size of the business will \textit{only be measured once at the time that the intermediary first makes an investment}, which is similar to how SBICs comply with the SBA’s size eligibility rules. Banks, otherwise, could potentially lose CRA credit qualification by helping small businesses grow, a result contrary to the goals of CRA. Limiting "economic development" to include only businesses with revenues of less than $5 million, moreover, omits an entire group of small businesses that still meet the size eligibility standards of the SBIC Program and that can create, retain, or improve jobs for low- or moderate-income (LMI) people or areas.

Jobs are an important CRA metric for Regulators and, pursuant to the first element of Question 13 in the Proposal, SBIA urges the retention of a separate jobs’ component metric under the "economic

\(^{7}\) CRA Rulemaking at 33900, 33898-33899. Regulators propose an important new distinction regarding the application of the term “economic development.” All reported direct bank lending to small businesses would be considered for CRA credit under the proposed Retail Lending Test, detailed at Section IX of the proposed regulation, not under the proposed “economic development” definition because Regulators seek to use the proposed CFPB Section 1071 standard that would define “small business” as those with $5 million or less in gross annual revenue.

\(^{8}\) 15 USC 661 (“It is declared to be the policy of the Congress and the purpose of this Act [Small Business Investment Act of 1958] to improve and stimulate the national economy in general and the small-business segment thereof in particular by establishing a program to stimulate and supplement the flow of private equity capital and long-term loan funds which small-business concerns need for the sound financing of their business operations and for their growth, expansion, and modernization, and which are not available in adequate supply: Provided, however, That this policy shall be carried out in such manner as to insure the maximum participation of private financing sources.”)

\(^{9}\) CRA Rulemaking at 34019 (text of proposed Sec. ___13(c)(2).)
development” definition. While this metric would apply only to bank investments in or loans to intermediaries that finance small businesses with gross annual revenues over $5 million, those small businesses should still meet the size and purpose standards under current CRA guidance, as opposed to focusing only on jobs for LMI persons as mentioned in Question 13. It would support job creation and retention and help more small businesses that already have trouble accessing capital. It would also help prevent a perverse incentive for smaller businesses not to grow in terms of revenues if such growth blocks access to capital because banks would have no incentive under CRA to make investments in intermediaries that fund them.

In response to the second element of Question 13, SBIA recommends retaining the SBIC program’s size eligibility standards to avoid eliminating CRA credit opportunities for bank investments in or loans to the type of non-SBIC financial intermediaries that meet the CRA’s current “size” and “purpose” tests.

Regarding the third element of Question 13 that asks whether there are criteria that demonstrate, essentially, that the primary purpose of a CRA credit eligible activity is job creation for LMI individuals, SBIA believes that Regulators should continue to use the two traditional methods of establishing “primary purpose” as set forth in current regulatory guidance and reiterated substantially in the Proposal.

There is no need to change a long-accepted practice that has worked well for more than two decades whereby CRA examiners “will employ appropriate flexibility in reviewing any information

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10 CRA Rulemaking at 33900 (“Question 13. Should the agencies retain a separate component for job creation, retention, and improvement for low- and moderate-income individuals under the economic development definition? If so, should activities conducted with businesses or farms of any size and that create or retain jobs for low- or moderate-income individuals be considered? Are there criteria that can be included to demonstrate that the primary purpose of an activity is job creation, retention, or improvement for low- or moderate-income individuals and that ensure activities are not qualified simply because they offer low wage jobs?)

11 The current regulatory guidance set forth in the Interagency Questions & Answers Regarding CRA at Section 12(g)(3)(1) contains both a “size” and “purpose” test. The “purpose” test specifically includes activities that either: (1) support “permanent job creation, retention, and/or improvement” (a) for low- or moderate-income (LMI) persons, (b) in LMI geographies, (c) in areas targeted for redevelopment by federal, state, local, or tribal government, (d) by financing intermediaries that lend to, invest in, or provide technical assistance to start-ups or recently formed small businesses, or (e) through technical assistance or supportive services for small businesses or farms, such as shared space, technology, or administrative assistance; or (2) support Federal, state, local, or tribal economic development initiatives that include provisions for creating or improving access by LMI persons to jobs or job training or workforce development programs.

12 Id.

13 See Interagency Questions & Answers Regarding CRA at Section 12(h)(8). (Describes two approaches: (1) if a majority of the dollars or beneficiaries of the activity are identifiable to one or more the enumerated community development purposes, then the activity will be considered to possess the requisite primary purpose; or (2) if the measurable portion of any benefit bestowed or dollars applied to community development purposes is a minority share of the activity’s total benefits or dollar value, then CRA credit may still be available for the entire activity if it is shown that (i) the bona fide intent/activity is primarily an enumerated community development purpose, and (ii) the activity is “specifically structured” to achieve the purpose(s), and (iii) the activity achieves or reasonable expects to achieve those community development purposes.)
provided by a financial institution that reasonably demonstrates that the purpose, mandate, or function of the activity meets the ‘purpose test’”. SBIA notes that the Proposal does not discuss why the Regulators are proposing to eliminate the jobs component so soon after expanding it in 2016, but SBIA urges the Regulators to stick to the strong policy underpinnings of their 2016 expansion of the jobs component of “economic development” such that jobs for LMI persons were retained as important but constituted only one out of the five factors of the “purpose” test. 15

II. Flexible Treatment for Geographic Allocation of Community Development Investment Dollars

SBIA supports the proposed geographic expansion – both inside and outside a bank’s facilities-based assessment areas - of zones for community development activities eligible for CRA credit, since some banks do not maintain as many physical branches as they did in the past and some have no branches at all. 16 Under the proposed regulations, banks will also be required to “collect and maintain, on an annual basis, data for loans and investments originated or purchased during the evaluation period and for loans and investments from prior years that are held on the bank’s balance sheet at the end of each quarter”. 17

SBIA, however, has material concerns about the proposed requirements that would force every dollar of a community development loan or investment to be geographically allocated down to the county level. 18

SBIA stipulates that it is outside our scope to comment on the specific recommendations and quantitative metrics proposed to designate assessment areas or measure retail lending by banks for CRA purposes. We urge Regulators, nevertheless, to extend a “flexible” approach to a bank’s community development investment activities because a bank’s community development investment activities are long-term deployments of capital into small businesses that can extend for years depending on the investment lifecycle of the investment fund. A bank’s capital commitment into an investment fund will extend well beyond the initial year of the commitment because unlike a retail loan, fund investment lifecycles are multi-year processes.

For CRA credit purposes, this distinction means that a bank’s commitment of capital into a fund will not equate with the geographic location of its final deployment into a particular small business. Depending on specific investment strategies, moreover, many funds also reserve between 15-25 percent of total capital commitments for “follow-on” investments that can be made years after the fund’s initial investment in a small business. For CRA credit purposes, this distinction means a bank’s capital cannot be tied precisely to geographic locations until the fund has deployed all of the capital commitments into underlying small businesses.

SBIA, therefore, urges regulators to permit maximum flexibility for banks to report their initial capital commitments for community development investments during a particular examination

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14 See Interagency Q&A at Sec. __, 12 (g)(3)-1.
15 See SBIA’s attached February 16, 2021, comment letter to the Federal Reserve’s ANPR for CRA reform.
16 CRA Rulemaking at 34022.
17 CRA Rulemaking at 34036.
18 CRA Rulemaking at 34053-34054 (Appendix B, Section 14).
period and then to amend those reports with geographic details necessary to reallocate CRA credit to specific assessment areas once deployment into particular small businesses has occurred.\(^{19}\)

For example, in the first year that a bank closes an investment in a fund, the bank would receive credit for the full amount of its investment reflected in the fund’s legal documents, and the fund manager could work with its bank investors to reflect the geography in which the fund reasonably expects to invest. Each year thereafter, the bank would receive CRA credit for the outstanding balance of that investment on the bank’s balance sheet, and fund managers could provide updated information with the location and amounts invested in each small business, which each bank investor would use to update its geographic allocations for that year.

Examiners should maintain a rule of reasonableness when evaluating a bank’s SBIC investments for CRA credit purposes and grant maximum flexibility for banks to apply those credits in whatever geography is most appropriate to ensure no CRA credit is left behind.\(^{20}\)

**III. Data Collection**

In response to the question by Regulators about other steps to take or procedures to develop to reduce the burden on banks to collect additional community development financing data, SBIA reminds Regulators to first identify and use data already collected before requiring new metrics.\(^{21}\)

For example, SBA already collects data from SBICs on a regular basis about job creation-retention by their portfolio companies (i.e., SBA Form 1031, SBA Portfolio Financing Report; SBA Form 468, SBA Annual Financial Report). Schedule 8 of the SBA Form 468 contains employment and other general data on the portfolio companies.\(^{22}\) Similarly, non-SBIC fund members of SBIA report that for many years they have assembled and provided to their bank investors documentation supporting the elements under the current “purpose” test, which the banks then in turn provided to their federal bank CRA examiners, with all bank investors receiving CRA credit for their investments.\(^{23}\)

SBIA urges the Regulators to be sensitive when considering imposing new data reporting obligations on banks about their community development investments because the underlying

\(^{19}\) See also Interagency Questions & Answers Regarding CRA at Sections __.12(h) – 6 (pertaining to bank investments in statewide or regional funds) and __.23(a) – 2 (pertaining to bank investments in nationwide funds). Regulators should also consider maintaining current regulatory guidance when the “purpose, mandate, or function” of the organization or activity includes serving geographies of individual located within the institution’s assessment area(s).

\(^{20}\) Additionally, SBIA strongly supports the proposed Section __.21(d) that would allow banks the option to choose to take pro-rata credit for a fund’s investments/loans into underlying portfolio companies or projects. CRA Rulemaking at 33926.

\(^{21}\) CRA Rulemaking at 34000 (“Question 162. What other steps can the agencies take, or what procedures can the agencies develop, to reduce the burden of the collection of additional community development financing data fields while still ensuring adequate data to inform the evaluation of performance? How could a data template be designed to promote consistency and reduce burden?)

\(^{22}\) See SBA SBIC forms at: https://www.sba.gov/sbic/sbic-resource-library/forms.

\(^{23}\) The documentation included a list of all small businesses their fund invested in, the location of each small business, applicable jobs and income data for each small business annually, and any other information relevant to the “purpose” test.
information still must come from small businesses. Small businesses, unlike large businesses, do not have the discretionary capital and administrative resources to meet onerous data reporting requirements. Burdensome requirements risk damage to small businesses because, in order to comply, they must reallocate limited resources of both staff time and money away from their principal activities that help create jobs and grow local economies.

SBIA encourages Regulators to first identify and inventory existing federal data sources and explore private sources of data before mandating new data metrics and reporting formats.

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SBIA commends federal regulators for their comprehensive approach to revise regulations governing the Community Reinvestment Act.

We applaud making express the long-standing presumption that bank investments in SBICs and RBICs qualify for CRA credit as economic development. With this clear distinction, there should no longer be any confusion among CRA examiners or regulated banks that all investments made through any form of SBIC and RBIC are eligible for full CRA credit.

As always, SBIA appreciates the invitation to discuss these issues and looks forward to the opportunity to work together to ensure America’s small businesses have access to the capital they need.

Sincerely,

Brett Palmer
SBIA President
February 16, 2021

BY ELECTRONIC TRANSMISSION

Ann E. Misback, Secretary
Board of Governors of the Federal Reserve System
20th St., and Constitution Ave., N.W.
Washington, D.C. 20551


Dear Ms. Misback:

On behalf of its membership, the Small Business Investor Alliance ("SBIA") is pleased to submit the following comments in response to the above-referenced advanced notice of proposed rulemaking by the Board of Governors of the Federal Reserve System ("Board") regarding modernizing the Board’s Community Reinvestment Act of 1977 ("CRA" or "Act") regulatory and supervisory framework codified at Regulation BB.

The SBIA is the national organization that represents small business funds and their investors, including Small Business Investment Companies ("SBICs"), some non-SBIC funds, and the many banks that invest in them. These funds make important contributions to job creation, retention, and improvement, and can provide a valuable vehicle for first-time fund managers, including founders of color and other emerging managers that may focus on early-stage small businesses.

SBICs are an outstanding example of the type of investments that are worthy of complete CRA consideration and scoring. SBICs, administered by the U.S. Small Business Administration ("SBA"), are highly regulated private funds that invest exclusively in domestic small businesses, which by statutory mission provide capital that is otherwise unavailable or in short supply to small businesses. An investment group that seeks an SBIC license must establish a record of not only solid investment performance, but also a record of being a good actor to the small businesses they have backed. SBICs may only provide long-term capital, not short-term lending, and must do so with a number of meaningful protections to the small business that otherwise would not be provided.

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1 12 U.S.C. 2901 et seq. The Board implements the CRA through Regulation BB. 12 CFR part 228.
Related, the U.S. Department of Agriculture ("USDA") operates the Rural Business Development Company (RBIC) program, a developmental venture capital program for the purpose of promoting economic development and the creation of wealth and job opportunities in non-metropolitan areas and among residents living in those areas. Like the SBA, the USDA licenses investment fund applicants to address the unmet capital needs of small enterprises primarily located in rural areas. The RBIC program does not offer its licensees federally guaranteed capital access like the SBIC program.

Together, however, SBICs and RBICs are capital engines for job creation and small business growth throughout the United States.

A recent independent study prepared for the Library of Congress found that SBIC-backed small businesses created almost 3 million new jobs and supported an additional 6.5 million jobs over the 20-year period of their study. Every one of the jobs created by each of those small businesses was a gain to the communities where they are located and to the broader regions from where they drew employees and to whom they provided goods and services. These businesses and jobs continue on, succeeding independently of SBICs after the investment is completed. These small businesses are not “propped up” or subsidized but transformed into stronger businesses because of SBIC investments.

The Board’s current CRA regulatory framework emphasizes the importance of SBICs and RBICs by expressly including them on the list of types of entities into which a bank loan or investment will be “presumed” to promote economic development and thus satisfy the “purpose” test without have to submit any further documentation.

SBIA presents the following comments to help inform the Board in its work to draft proposed amendments to its current CRA regulatory framework that governs its regulated financial institutions. In general, SBIA offers the following recommendations:

- Retain all of the current categories and types of activities and entities that currently qualify for CRA credit under the current regulatory framework for the “promotion of economic development,” including the express inclusion of SBICs and RBICs on the list of entities “presumed” to promote economic development.
- Do not revise the current small business size standards. Rather, SBIA suggests that, as outlined below, the current CRA regulatory framework can be enhanced to promote increased loans to or investments in the “smallest businesses” and also minority-owned small businesses.

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4 Interagency Questions & Answers Regarding Community Reinvestment ("CRA Interagency Q&A") at Sec. 12(g)(3)-1.
The Story of Small Business Investment Companies (SBICs)

SBICs are an American success story and example of a successful federal public policy that aligns the power of private markets with the public interest of job creation and economic growth.

Congress declared in its original authorizing legislation that the SBIC program should “stimulate and supplement the flow of private equity capital and long-term loan funds which small business concerns need for the sound financing of their business operations” while also stimulating the national economy and job growth.\(^5\)

As of the first quarter of 2021, the SBIC program has grown to a combined SBA guaranteed and private capital program exceeding $33 billion, an increase of 19 percent since 2016 and the highest level ever in program history.\(^6\) SBICs completed $630 million in financings to small businesses in December 2020, which was a 25 percent jump from $500 million in December 2019.\(^7\)

At the end of fiscal year 2020, the SBIC program included more than 300 licensed funds.\(^8\) Over the last five fiscal years, on average, SBICs have invested nearly $6 billion annually in over 1,100 small businesses, creating or sustaining nearly 109,000 jobs annually.\(^9\) Fifty-five (55%) percent of SBIC investments were made in small businesses that were either women-, minority- or veteran-owned, located in LMIs areas, or were special competitive opportunity gap businesses.\(^10\)

SBICs invest exclusively in domestic small businesses, creating jobs and empowering U.S. small businesses to compete in a global economy. SBICs may not invest in certain sectors (e.g., real estate; project financing; farmland) and may not make investments in companies that offshore jobs; SBICs may not finance any business “contrary to the public interest, including but not limited to activities which are in violation of law, or inconsistent with free competitive enterprise”.\(^11\)

Companies that in their early stages received SBIC investments and have subsequently grown into icons of American industry include Federal Express, Apple, Intel, and Callaway Golf. While these are recognized companies globally, many more small businesses backed by SBICs have grown from smaller businesses into robust, sustainable mid-sized businesses.

\(^5\) Supra Note 2.
\(^7\) Id.
\(^9\) Id. SBA estimates jobs created or sustained using “The 1999 Arizona Venture Capital Impact Study” (confirmed by the DRI-WEFA study of 2001) whereby one (1) job is created for every $36,000 of SBIC investment (adjusted for inflation).
\(^10\) Id.
SBICs were essential not only to the success but, in certain cases, survival of these smaller businesses that bring prosperity, employment, and hope to communities across the country, many in LMI and underserved markets, because there were no other sources of capital available to them.

These investments are in real companies with real staying power and real growth potential.

i. **SBIC Program Structure and Function:**

The SBIC program is a market-driven platform that serves an important public purpose of facilitating private investment into and filling capital access gaps for domestic small businesses. The program was created in 1958 during the Glass-Steagall era. SBIC investments by banks are specifically and clearly permitted in statute in the Dodd-Frank Act, as they were under Glass-Steagall.

SBICs are federally regulated, privately-owned and managed investment funds that invest exclusively in domestic small business. SBICs, primarily formed as limited partnerships, provide long-term loans, equity investments, or both along with management assistance to small businesses across a range of sectors, geographic locations, and stages of growth. Some SBICs specialize in an industry sector while others invest more broadly. There are various forms of SBICs:

- **Leveraged (Debenture) SBICs** increase the amount of capital available for domestic small business investing by accessing the SBIC credit facility. SBIC leverage is borrowed at the fund level, not at the small business level.

- **Non-levered SBICs** do not seek or receive SBA leverage. Non-levered funds can provide debt, equity, or both. They are able to provide more equity to small businesses than levered (debenture) SBIC funds because they do not need to make interest payments on SBIC leverage. Banks commonly invest a portion of their own capital into these funds. These funds present no taxpayer risk because there are no public funds or federal guarantees involved.

- **Bank-Owned SBICs** are fully owned or funded by a single bank. Like other non-levered SBIC funds, they do not access leverage and have no taxpayer risk. Like other non-levered SBICs, these bank-owned SBICs can provide debt or equity. Since these SBICs are unlevered, they are able to provide more equity because they do not have interest payments to make on SBIC leverage.
Most SBICs are levered (debenture) funds. These levered SBICs invest private capital that is amplified by access to an SBA-backed credit facility using the Federal Home Loan Bank system. This permits individual SBICs to multiply paid-in private capital up to three-times capital or $175 million, whichever is less. In exchange for accessing federal leverage, SBICs limit themselves in a number of ways including to investing only in domestic small businesses. The performance of the SBIC debentures is guaranteed by the federal government, but not the performance of any single SBIC investment or the SBIC fund itself.

The maximum leverage for an SBIC family of funds (a group that hold multiple SBIC licenses) is currently $350 million. Three times leverage is the statutory limit, which is rarely used and which the SBA will only permit under unusual circumstances. Most levered SBIC funds lever private capital one to two times their private capital. For example, an SBIC may raise $87.5 million in private capital and then, after licensure, may access up to an additional $175 million line of credit (SBA leverage), which combines for a total of $262.5 million – a very large boost in the small business economy. The leverage is provided at a zero-subsidy rate, with no annual appropriations necessary to fund up to $4 billion a year in SBIC leverage, which is eventually paid back in full to the SBA with interest and fees.

Real economic development continues positive economic impacts well beyond the time of initial deployment of capital. Successful small business investing continues to support the community with jobs and local taxes for many years.

**CRA Community Development Subcomponents – “Economic Development”**

The Board’s current CRA regulatory framework expressly recognizes the critical role that small businesses play in the United States in its definition of “community development,” which captures:

> ...activities that promote economic development by financing businesses or farms that meet the size eligibility standards of the Small Business Administration’s Development Company or Small Business Investment company program (13 CFR 121.301) or have gross annual revenues of $1 million or less.\(^\text{12}\)

In addition to this “size” test, the current CRA framework also outlines a “purpose” test, focused primarily on activities that support: (1) jobs for low- or moderate-income (LMI) people, in LMI communities, in areas targeted for redevelopment, by financing intermediaries that lend to or invest in start-ups or recently formed small businesses, and through various types of technical assistance or supportive services for small businesses or farms; or, (2) federal, state, local, or tribal economic development initiatives focused on creating or improving access by low- or moderate-income persons to jobs or job training or workforce development programs.\(^\text{13}\)

\(^{12}\) 12 CFR 12(g)(3).
\(^{13}\) CRA Interagency Q&As at Sec. ___12(g)(3)-1.
As mentioned above, the CRA framework emphasizes the importance of SBICs by expressly including them on the list of types of entities into which a bank loan or investment will be “presumed” to promote economic development and thus satisfy the “purpose” test without having to submit any further documentation.\textsuperscript{14}

In 2016, the three federal regulators of financial institutions, the Board, the Federal Deposit Insurance Corporation (FDIC), and the Office of the Comptroller of the Currency (OCC), revised their CRA Interagency Q&A to expand the “promotion of economic development” prong of the definition of community development. The 2016 guidance contained compelling policy discussions about small businesses and economic development and provided strong support for expanding the categories of the “purpose” test.

SBIA agrees with the policy underpinnings of the CRA Interagency Q&A and strongly urges the Board not to second-guess its 2016 guidance on the interpretation and application regarding the “promoting economic development” prong.

We counsel the Board, especially during this period of economic dislocation, to retain all of the current variety of qualified methods for a financial institution to demonstrate that its community development activities promote economic development, and to re-emphasize its language from the 2016 guidance that “[CRA] examiners will employ appropriate flexibility in reviewing any information provided by a financial institution that reasonably demonstrates that the purpose, mandate, or function of an [CRA qualifying] activity meets the purpose test.”\textsuperscript{15} (emphasis added).

Specifically, the Board seeks responses to the following questions:

- \textbf{Question 57. What other options should the Board consider for revising the economic development definition to provide incentives for engaging in activity with smaller businesses and farms and/or minority-owned businesses?}
  
  i. \textit{“Responsiveness” Option:}

The Board is considering specifying that “economic development activity with the smallest businesses...as well as minority-owned small businesses would be considered responsive and impactful” in developing a CD conclusion of rating per bank.\textsuperscript{16}

\textsuperscript{14} Id.

\textsuperscript{15} 81 FedReg 48508 (July 25, 2016). The CRA Interagency Q&A then gave additional guidance about qualitative aspects of demonstrating the “purpose” test. “Examiners will also consider the qualitative aspects of performance. For example, activities will be considered more responsive to community needs if a majority of jobs created, retained, and/or improved, benefit low- or moderate-income individuals.”

\textsuperscript{16} 85 FedReg 66446 (Oct. 19, 2020).
The Board proffers no proposed definition for “smaller businesses” or metrics for “responsiveness”. The “responsiveness” option would make no changes to the business size standards that apply to existing qualifying activities like SBIC or RBIC investments, but the Board notes its concern that this option “might provide insufficient incentives” for banks to engage in activities with smaller businesses and minority-owned smaller businesses.¹⁷

SBIA acknowledges the Board’s concerns about access to credit for the “smallest segment of small business,” but counsels the Board to examine existing regulations that govern the SBIC and RBICs programs because they are directly on point.¹⁸

In addition to owning and financing small businesses, an SBIC licensed since 2009 must have 25 percent (in dollars) of its financings in "smaller enterprises".¹⁹ SBICs that are out of compliance have until the end of the following fiscal year to do so, or the SBIC will not be eligible for additional federal leverage.²⁰ USDA regulations require that more than 50 percent of RBIC financings (in total dollars) must go to “smaller enterprises” that meet either a net worth/net income or size standard test.²¹ Like SBICs, RBICs that are non-compliant have until the end of the following fiscal year to do so.²²

"Small enterprises" are defined for both SBICs and RBICs as companies with a net worth not in excess of $6 million, and a net income after taxes not in excess of $2 million for the preceding two fiscal years.²³

SBIA reminds the Board that SBICs and RBICs are already responsive to smaller businesses and recommends that the Board evaluate for CRA purposes existing SBA and USDA regulations, definitions, and specific metrics.

ii. Narrowing the Size Standard:

The Board is considering narrowing the scope of CRA credit eligibility to bank investments in only the “smallest” small businesses and farms by using just the revised gross annual revenue threshold and eliminating the SBIC and SBDC size standards.

SBIA strongly opposes this option because this would exclude and essentially redefine down “small business” to just “smaller businesses” which would chill job creation, risk damaging more small businesses, and run counter to the 60-plus years of federal policy supporting the SBIC program.

¹⁷ Id. at 66447.
¹⁸ 85 FedReg 66446 (fn 135) (2020)
¹⁹ 13 CFR 107.710. The percentage requirement is adjusted slightly for levered and non-levered SBICs licensed prior to 2009.
²⁰ See 13 CFR §107.1120(c) and (g).
²¹ 7 CFR 4290.700 (a)(2).
²² Id. (USDA warns non-compliant RBICs that “[t]or as long as you remain out of compliance, you are not eligible for additional Leverage (see § 4290.1120).”)
²³ 13 CFR 107.710 and 7 CFR 4209.50.
This narrow approach stands in opposition to the purpose of the CRA “to encourage regulated financial institutions to help meet the credit needs of their entire communities” (emphasis added).\textsuperscript{24} It would have the unintended consequence of shutting off essential access to capital for small businesses with annual gross revenues over $1 million generally because it would remove an important incentive for bank investments in those recipients.\textsuperscript{25} Related, it would create a perverse incentive for smaller businesses not to grow in terms of new jobs and revenues if graduation from the “smaller business” designation blocks access to capital because banks would have no incentive under the CRA to make investments in them.

Eliminating activities that currently qualify for CRA consideration is a risk that the Board admits is in play should it proceed to qualify economic development activities using only a revised gross annual revenue threshold.\textsuperscript{26} But for the CRA consideration, bank investments in SBICs would become less advantageous for them to make.

Without investments from SBICs that qualify for CRA consideration, which would be lost under this option, all small businesses risk a reduction in their access to capital.

SBIA suggests that, instead of narrowing the “size” standard, a more appropriate way to encourage more lending to and investments in the smallest businesses and minority-owned small businesses would be to enhance the current CRA framework by adding them to the list of entities that are “presumed” to promote economic development. This would also relieve those small businesses from the data collection burden sometimes associated with proving that they meet the “purpose” test.

Given the damage to the small business economy and resulting jobs losses from the pandemic, reducing access to capital with overly restrictive investment practices would lead to stunted job creation and extended economic dislocation.

- **Question 58.** How could the Board establish clearer standards for economic development activities to “demonstrate LMI job creation, retention, or improvement”?

The Board seeks ways to “provide more clarity” on the standard that financing activities for small businesses (and not just the undefined category of “smaller businesses”) show LMI job creation, retention, or improvement. The Board seeks recommendations about how to quantify and document jobs creation progress.

\textsuperscript{24} 81 FedReg 48506 (July 25, 2016).

\textsuperscript{25} Supra Note 3 at 13-14 and 20 (“Comparing SBICs to the overall private equity universe, SBICs invest in portfolio companies that are smaller and potentially less profitable on average. This can be seen by comparing the average portfolio company revenues across all private capital funds (US$404.3 million) to the average for all active SBICs (US$31.6 million). Even compared to funds less than or equal to US$225 million, for which average portfolio company revenues are US$180.5 million, SBIC funds invest in smaller companies.”)

\textsuperscript{26} 85 FedReg 66447 (“The Board recognizes that a possible drawback to using only a revised gross annual revenue threshold is that certain currently eligible activities that qualify under the economic development definition might no longer qualify for (CRA credit) consideration.”) (Oct. 19, 2020).
SBIA encourages the Board to survey current federal data collection sources and practices because the issue is not identifying new standards but finding reliable metrics to measure those standards. SBA collects data from SBICs on a regular basis about job creation-retention by their portfolio companies (i.e., SBA Form 1031, SBA Portfolio Financing Report; SBA Form 468, SBA Annual Financial Report). For instance, Schedule 8 of the SBA Form 468 contains employment and other general data on the portfolio companies.27

Similarly, non-SBIC fund members of SBIA report that for many years they have assembled and provided to their bank investors clear documentation of the “purpose” test, which the banks then in turn provided to their federal bank CRA examiners, with all bank investors receiving CRA for their investments.28 Identifying and inventoring existing federal data sources and, exploring private sources of data, would be a better use of limited federal dollars and personnel than setting new standards.

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During the current economic dislocation caused by the Covid pandemic, expanding or, at minimum maintaining, not narrowing, the application and interpretation of the “promoting economic development” prong signals to financial institutions that they should be creative and nimble in extending capital to all qualifying small businesses, including the smallest ones, and especially those in LMI.

As always, SBIA appreciates the opportunity to discuss these issues and looks forward to the opportunity to work together to update applicable regulations to ensure America’s small businesses have access to the capital they need.

Sincerely,

Brett Palmer
SBIA President

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27 See SBA SBIC forms at: https://www.sba.gov/sbic/sbic-resource-library/forms.
28 The documentation included a list of all small businesses their fund invested in, the location of each small business, applicable jobs and income data for each small business annually, and any other information relevant to the “purpose” test.