

§ 120.400

13 CFR Ch. I (1–1–10 Edition)

(u) *Personal resources test.* The personal resources test provisions of § 120.102 do not apply to ARC Loans.

(v) *Statutory loan limit.* The provisions of § 120.151 do not apply to ARC Loans.

[74 FR 27247, June 9, 2009]

Subpart D—Lenders

§ 120.400 Loan Guarantee Agreements.

SBA may enter into a Loan Guarantee Agreement with a Lender to make deferred participation (guaranteed) loans. Such an agreement does not obligate SBA to participate in any specific proposed loan that a Lender may submit. The existence of a Loan Guarantee Agreement does not limit SBA's rights to deny a specific loan or establish general policies. *See also* §§ 120.441(b) and 120.451(d) concerning Supplemental Guarantee Agreements.

PARTICIPATION CRITERIA

§ 120.410 Requirements for all participating Lenders.

A Lender must:

(a) Have a continuing ability to evaluate, process, close, disburse, service, liquidate and litigate small business loans including, but not limited to:

(1) Holding sufficient permanent capital to support SBA lending activities (for SBA Lenders with a Federal Financial Institution Regulator, meeting capital requirements for an adequately capitalized financial institution is considered sufficient permanent capital to support SBA lending activities; for SBLCs, meeting its SBA minimum capital requirement; and for NFRLs, meeting its state minimum capital requirement); and

(2) Maintaining satisfactory SBA performance, as determined by SBA in its discretion. The 7(a) Lender's Risk Rating, among other factors, will be considered in determining satisfactory SBA performance. Other factors may include, but are not limited to, on-site review/examination assessments, historical performance measures (like default rate, purchase rate and loss rate), loan volume to the extent that it impacts performance measures, and other performance related measurements and

information (such as contribution toward SBA mission);

(b) Be open to the public for the making of such loans (not be a financing subsidiary, engaged primarily in financing the operations of an affiliate);

(c) Have continuing good character and reputation, and otherwise meet and maintain the ethical requirements of § 120.140

(d) Be supervised and examined by either:

(1) A Federal Financial Institution Regulator,

(2) A state banking regulator satisfactory to SBA, or

(3) SBA;

(e) Be in good standing with SBA as defined in § 120.420(f) (and determined by SBA in its discretion) and, as applicable, with an SBA Lender's state regulator and Federal Financial Institution Regulator; and

(f) Operate in a safe and sound condition using commercially reasonable lending policies, procedures, and standards employed by prudent Lenders.

[61 FR 3235, Jan. 31, 1996, as amended at 62 FR 302, Jan. 3, 1997; 73 FR 75510, Dec. 11, 2008]

§ 120.411 Preferences.

An agreement to participate under the Act may not establish any Preferences in favor of the Lender.

§ 120.412 Other services Lenders may provide Borrowers.

Subject to § 120.140 Lenders, their Associates or the designees of either may provide services to and contract for goods with a Borrower only after full disbursement of the loan to the small business or to an account not controlled by the Lender, its Associate, or the designee. A Lender, an Associate, or a designee providing such services must do so under a written contract with the small business, based on time and hourly charges, and must maintain time and billing records for examination by SBA. Fees cannot exceed those charged by established professional consultants providing similar services. *See also* § 120.195.

Small Business Administration

§ 120.420

§ 120.413 Advertisement of relationship with SBA.

A Lender may refer in its advertising to its participation with SBA. The advertising may not:

- (a) State or imply that the Lender, or any of its Borrowers, has or will receive preferential treatment from SBA;
- (b) Be false or misleading; or
- (c) Make use of SBA's seal.

PARTICIPATING LENDER FINANCINGS

SOURCE: Sections 120.420 through 120.428 appear at 64 FR 6507-6509, Feb. 10, 1999, unless otherwise noted.

§ 120.420 Definitions.

(a) *7(a) Loans*—All references to 7(a) loans under this subpart include loans made under section 7(a) of the Small Business Act (15 U.S.C. 631 *et seq.*) and loans made under section 502 of the Small Business Investment Act (15 U.S.C. 661 *et seq.*), both of which may be securitized under this subpart.

(b) *Bank Regulatory Agencies*—The bank regulatory agencies are the Federal Deposit Insurance Corporation, the Federal Reserve Board, the Office of the Comptroller of the Currency, and the Office of Thrift Supervision.

(c) *Benchmark Number*—The maximum number of percentage points that a securitizer's Currency Rate can decrease without triggering the PLP suspension provision set forth in §120.425. SBA will publish the Benchmark Number in the FEDERAL REGISTER.

(d) *Currency Rate*—A securitizer's "Currency Rate" is the dollar balance of its 7(a) guaranteed loans that are less than 30 days past due divided by the dollar balance of its portfolio of 7(a) guaranteed loans outstanding, as calculated quarterly by SBA, excluding loans approved in SBA's current fiscal year.

(e) *Currency Rate Percentage*—The relationship between the securitizer's Currency Rate and the SBA 7(a) loan portfolio Currency Rate as calculated by dividing the securitizer's Currency Rate by the SBA 7(a) loan portfolio Currency Rate.

(f) *Good Standing*—In general, a Lender is in "good standing" with SBA if it:

(1) Is in compliance with all applicable:

- (i) Laws and regulations;
- (ii) Policies; and
- (iii) Procedures;

(2) Is in good financial condition as determined by SBA;

(3) Is not under investigation or indictment for, or has not been convicted of, or had a judgment entered against it for felony or fraud, or charges relating to a breach of trust or violation of a law or regulation protecting the integrity of business transactions or relationships, unless the Lender Oversight Committee has determined that good standing exists despite the existence of such factors.

(4) Does not have any officer or employee who has been under investigation or indictment for, or has been convicted of or had a judgment entered against him for, a felony or fraud, or charges relating to a breach of trust or violation of a law or regulation protecting the integrity of business transactions or relationships, unless the Lender Oversight Committee has determined that good standing exists despite the existence of such person.

(g) *Initial Currency Rate*—The Initial Currency Rate (ICR) is the securitizer's benchmark Currency Rate. SBA will calculate the securitizer's ICR as of the end of the calendar quarter immediately prior to the first securitization completed after April 12, 1999. This calculation will include all 7(a) loans which are outstanding and were approved in any fiscal year prior to SBA's current fiscal year. Each quarter, SBA will compare each securitizer's Currency Rate to its ICR.

(h) *Initial Currency Rate Percentage*—The Initial Currency Rate Percentage (ICRP) measures the relationship between a securitizer's Initial Currency Rate and the SBA 7(a) loan portfolio Currency Rate at the time of the first securitization after April 12, 1999. The ICRP is calculated by dividing the securitizer's Currency Rate by the SBA 7(a) loan portfolio Currency Rate. SBA will calculate the securitizer's ICRP as of the end of the calendar quarter immediately prior to the first securitization completed after April 12, 1999.

§ 120.421

(i) *Loss Rate*—A securitizer’s “loss rate,” as calculated by SBA, is the aggregate principal amount of the securitizer’s 7(a) loans determined uncollectable by SBA for the most recent 10-year period, excluding SBA’s current fiscal year activity, divided by the aggregate original principal amount of 7(a) loans disbursed by the securitizer during that period.

(j) *Nondepository Institution*—A “non-depository institution” is a Small Business Lending Company (“SBLC”) regulated by SBA or a Business and Industrial Development Company (“BIDCO”) or other nondepository institution participating in SBA’s 7(a) program.

(k) *Securitization*—A “securitization” is the pooling and sale of the unguaranteed portion of SBA guaranteed loans to a trust, special purpose vehicle, or other mechanism, and the issuance of securities backed by those loans to investors in either a private placement or public offering.

[64 FR 6507–6509, Feb. 10, 1999, as amended at 73 FR 75511, Dec. 11, 2008]

§ 120.421 Which Lenders may securitize?

All SBA participating Lenders may securitize subject to SBA’s approval.

§ 120.422 Are all securitizations subject to this subpart?

All securitizations are subject to this subpart. Until additional regulations are promulgated, SBA will consider securitizations involving multiple Lenders on a case by case basis, using the conditions in §120.425 as a starting point. SBA will consider securitizations by affiliates as single Lender securitizations for purposes of this subpart.

§ 120.423 Which 7(a) loans may a Lender securitize?

A Lender may only securitize 7(a) loans that will be fully disbursed within 90 days of the securitization’s closing date. If the amount of a fully disbursed loan increases after a securitization settles, the Lender must retain the increased amount.

13 CFR Ch. I (1–1–10 Edition)

§ 120.424 What are the basic conditions a Lender must meet to securitize?

To securitize, a Lender must:

(a) Be in good standing with SBA as defined in §120.420(f) of this chapter and determined by SBA in its discretion;

(b) Have satisfactory SBA performance, as determined by SBA in its discretion. The Lender’s Risk Rating, among other factors, will be considered in determining satisfactory SBA performance. Other factors may include, but are not limited to, on-site review/examination assessments, historical performance measures (like default rate, purchase rate and loss rate), loan volume to the extent that it impacts performance measures, and other performance related measurements and information (such as contribution toward SBA mission);

(c) Use a securitization structure which is satisfactory to SBA;

(d) Use documents acceptable to SBA, including SBA’s model multi-party agreement, as amended from time to time;

(e) Obtain SBA’s written consent, which it may withhold in its sole discretion, prior to executing a commitment to securitize; and

(f) Cause the original notes to be stored at the FTA, as defined in §120.600, and other loan documents to be stored with a party approved by SBA.

[64 FR 6507–6509, Feb. 10, 1999, as amended at 73 FR 75511, Dec. 11, 2008]

§ 120.425 What are the minimum elements that SBA will require before consenting to a securitization?

A securitizer must comply with the following three conditions:

(a) *Capital Requirement*—All securitizers must be considered to be “well capitalized” by their regulator. SBA will consider a depository institution to be in compliance with this section if it meets the definition of “well capitalized” used by its bank regulator. SBA’s capital requirement does not change the requirements that banks already meet. For nondepository institutions, SBA, as the regulator, will consider a non-depository institution to be “well capitalized” if it maintains a minimum unencumbered paid in capital and paid in surplus equal to

at least 10 percent of its assets, excluding the guaranteed portion of 7(a) loans. The capital charge applies to the remaining balance outstanding on the unguaranteed portion of the securitizer's 7(a) loans in its portfolio and in any securitization pools. Each nondepository institution must submit annual audited financial statements demonstrating that it has met SBA's capital requirement.

(b) **Subordinated Tranche**—A securitizer or its wholly owned subsidiary must retain a tranche of the securities issued in the securitization (subordinated tranche) equal to the greater of two times the securitizer's Loss Rate or 2 percent of the principal balance outstanding at the time of securitization of the unguaranteed portion of the loans in the securitization. This tranche must be subordinate to all other securities issued in the securitization including other subordinated tranches. The securitizer or its wholly owned subsidiary may not sell, pledge, transfer, assign, sell participations in, or otherwise convey the subordinated tranche during the first 6 years after the closing date of the securitization. The securities evidencing the subordinated tranche must bear a legend stating that the securities may not be sold until 6 years after the issue date. SBA's Securitization Committee may modify the formula for determining the tranche size for a securitizer creating a securitization from a pool of loans located in a region affected by a severe economic downturn if the Securitization Committee concludes that enforcing this section might exacerbate the adverse economic conditions in the region. SBA will work with the securitizer to verify the accuracy of the data used to make the Loss Rate calculation.

(c) **PLP Privilege Suspension.**

(1) *Suspension:* If a securitizer's Currency Rate declines, SBA may suspend the securitizer's PLP unilateral loan approval privileges (PLP approval privileges) if the decline from the securitizer's ICR is more than the Benchmark Number as published in the FEDERAL REGISTER from time to time and the securitizer's Currency Rate Percentage is less than its ICRP. The securitizer will first be placed on pro-

bation for one quarter. If, at the end of the probationary quarter the securitizer has not met either of the following conditions in paragraph (c)(1)(i) or (c)(1)(ii) of this section, SBA will suspend the securitizer's PLP approval privileges and will not approve additional securitization requests from that securitizer. SBA will provide written notice at least 10 days prior to the effective date of suspension. The suspension will last a minimum of 3 months. During the suspension period, the securitizer must use Certified Lender or Regular Procedures to process 7(a) loan applications. The prohibition will end if, at the end of the probationary quarter: (i) the securitizer has improved its Currency Rate to above its ICR less the Benchmark Number; or (ii) its Currency Rate Percentage is either the same or greater than its ICRP.

(2) *Reinstatement:* The suspension will remain in effect until the securitizer meets either the condition in paragraph (c)(1)(i) or (c)(1)(ii) of this section. If the securitizer meets either condition by the end of the 3-month period, notifies SBA with acceptable documentation, and SBA agrees, SBA will reinstate the securitizer. If the securitizer cannot meet either condition, the suspension will remain in effect. The securitizer may then petition the Lender Oversight Committee (Committee) for reinstatement. The Committee will review the reinstatement petition and determine if the securitizer's PLP approval privilege and securitization status should be reinstated. The Committee may consider the economic conditions in the securitizer's market area, the securitizer's efforts to improve its Currency Rate, and the quality of the securitizer's 7(a) loan packages and servicing. The Committee will consider only one petition by a securitizer per quarter.

(3) *The Benchmark Number.* SBA will monitor the Benchmark Number. If economic conditions or policy considerations warrant, SBA may modify the Benchmark Number to protect the safety and soundness of the 7(a) program.

(4) *Data.* SBA will calculate Currency Rate and Currency Rate Percentages quarterly from financial information

§ 120.426

that securitizers provide. SBA will work with a securitizer to verify the accuracy of the data used to make the Currency Rate calculation.

[64 FR 6508, Feb. 10, 1999, as amended at 65 FR 49481, Aug. 14, 2000; 73 FR 75511, Dec. 11, 2008]

§ 120.426 What action will SBA take if a securitizer transfers the subordinated tranche prior to the termination of the holding period?

If a securitizer transfers the subordinated tranche prior to the termination of the holding period, SBA will suspend immediately the securitizer's ability to make new 7(a) loans. The securitizer will have 30 calendar days to submit an explanation to Lender Oversight Committee ("Committee"). The Committee will have 30 calendar days to review the explanation and determine whether to lift the suspension. If an explanation is not received within 30 calendar days or the explanation is not satisfactory to the Committee, SBA may transfer the servicing of the applicable securitized loans, including the securitizers' servicing fee on the guaranteed and unguaranteed portions and the premium protection fee on the guaranteed portion, to another SBA participating Lender.

[64 FR 6507-6509, Feb. 10, 1999, as amended at 73 FR 75511, Dec. 11, 2008]

§ 120.427 Will SBA approve a securitization application from a capital impaired Securitizer?

If a securitizer does not maintain the level of capital required by this subpart, SBA will not approve a securitization application from that securitizer.

§ 120.428 What happens to a securitizer's other PLP responsibilities if SBA suspends its PLP approval privilege?

The securitizer must continue to service and liquidate loans according to its PLP Supplemental Agreement.

OTHER CONVEYANCES

SOURCE: Sections 120.430 through 120.435 appear at 64 FR 6509, 6510, Feb. 10, 1999, unless otherwise noted.

13 CFR Ch. I (1-1-10 Edition)

§ 120.430 What conveyances are covered by §§ 120.430 through 120.435?

Sections 120.430 through 120.435 cover all other transactions in which a Lender sells, sells a participating interest in, or pledges an SBA guaranteed loan other than for the purpose of securitizing and other than conveyances covered under Subpart F, Secondary Market, of this part.

§ 120.431 Which Lenders may sell, sell participations in, or pledge 7(a) loans?

All Lenders may sell, sell participations in, or pledge 7(a) loans in accordance with this subpart.

§ 120.432 Under what circumstances does this subpart permit sales of, or sales of participating interests in, 7(a) loans?

(a) A Lender may sell all of its interest in a 7(a) loan to another Lender operating under a current Loan Guarantee Agreement (SBA Form 750) ("participating Lender"), with SBA's prior written consent, which SBA may withhold in its sole discretion. A Lender may not sell any of its interest in a 7(a) loan to a nonparticipating Lender. The purchasing Lender must take possession of the promissory note and other loan documents, and service the sold 7(a) loan. The purchasing Lender purchases the loan subject to SBA's existing rights including its right to deny liability on its guarantee as provided in §120.524. After purchase, the purchased loan will be subject to the purchasing Lender's Loan Guarantee Agreement.

(b) A Lender may sell, or sell a participating interest in, a part of a 7(a) loan to another participating Lender. If the Lender retains ownership of a part of the unguaranteed portion of the loan equal to at least 10 percent of the outstanding principal balance of the loan, the Lender must give SBA prior written notice of the transaction, and the Lender must continue to hold the note and service the loan. If a Lender retains ownership of a part of the unguaranteed portion of the loan equal to less than 10 percent of the outstanding principal balance of the loan, the Lender must obtain SBA's prior written consent to the transaction,

Small Business Administration

§ 120.440

which consent SBA may withhold in its sole discretion. The Lender must continue to hold the note and other loan documents, and service the loan unless SBA otherwise agrees in its sole discretion.

(c) For purposes of determining the percentage of ownership a Lender has retained, SBA will not consider a Lender to be the owner of the part of a loan in which it has sold a participating interest.

§ 120.433 What are SBA's other requirements for sales and sales of participating interests?

SBA requires the following:

(a) The Lender must be in good standing with SBA as defined in § 120.420(f) and determined by SBA in its discretion;

(b) The Lender has satisfactory SBA performance, as determined by SBA in its discretion. The Lender's Risk Rating, among other factors, will be considered in determining satisfactory SBA performance. Other factors may include, but are not limited to, on-site review/examination assessments, historical performance measures (like default rate, purchase rate and loss rate), loan volume to the extent that it impacts performance measures, and other performance related measurements and information (such as contribution toward SBA mission); and

(c) In transactions requiring SBA's consent, all documentation must be satisfactory to SBA, including, if SBA determines it to be necessary, a multi-party agreement.

[64 FR 6507-6509, Feb. 10, 1999, as amended at 73 FR 75511, Dec. 11, 2008]

§ 120.434 What are SBA's requirements for loan pledges?

(a) Except as set forth in § 120.435, SBA must give its prior written consent to all pledges of any portion of a 7(a) loan, which consent SBA may withhold in its sole discretion;

(b) The Lender must be in good standing with SBA as defined in § 120.420(f) and determined by SBA in its discretion;

(c) The Lender has satisfactory SBA performance, as determined by SBA in its discretion. The Lender's Risk Rating, among other factors, will be con-

sidered in determining satisfactory SBA performance. Other factors may include, but are not limited to, on-site review/examination assessments, historical performance measures (like default rate, purchase rate and loss rate), loan volume to the extent that it impacts performance measures, and other performance related measurements and information (such as contribution toward SBA mission);

(d) All loan documents must be satisfactory to SBA and must include a multi-party agreement among SBA, Lender, the pledgee, FTA and such other parties as SBA determines are necessary;

(e) The Lender must use the proceeds of the loan secured by the 7(a) loans only for financing 7(a) loans and for costs and expenses directly connected with the borrowing for which the loans are pledged;

(f) The Lender must remain the servicer of the loans and retain possession of all loan documents other than the original promissory notes;

(g) The Lender must deposit the original promissory notes at the FTA; and

(h) The Lender must retain an economic interest in and the ultimate risk of loss on the unguaranteed portion of the loans.

[64 FR 6507-6509, Feb. 10, 1999, as amended at 73 FR 75511, Dec. 11, 2008]

§ 120.435 Which loan pledges do not require notice to or consent by SBA?

Notwithstanding the provisions of § 120.434(e), 7(a) loans may be pledged for the following purposes without notice to or consent by SBA:

- (a) Treasury tax and loan accounts;
- (b) The deposit of public funds;
- (c) Uninvested trust funds;
- (d) Discount borrowings at a Federal Reserve Bank; or
- (e) Advances by a Federal Home Loan Bank.

[64 FR 6507-6509, Feb. 10, 1999, as amended at 73 FR 75511, Dec. 11, 2008]

CERTIFIED LENDERS PROGRAM (CLP)

§ 120.440 The Certified Lenders Program.

Under the Certified Lenders Program (CLP), designated Lenders process and

§ 120.441

13 CFR Ch. I (1–1–10 Edition)

close 7(a) loans and service and liquidate such loans in accordance with subpart E of this part. SBA gives priority to applications and servicing actions submitted by Lenders under this program, and will provide expedited loan processing or servicing. All other rules in this part 120 relating to the operations of Lenders apply to CLP Lenders.

[61 FR 3235, Jan. 31, 1996; 61 FR 7986, Mar. 1, 1996, as amended at 72 FR 18360, Apr. 12, 2007]

§ 120.441 How does a Lender become a CLP Lender?

(a) An SBA field office may nominate a Lender or a Lender may request a field office to consider it for CLP status. SBA district directors may approve and renew a Lender's CLP status. The district director will consider whether the Lender:

(1) Has the ability to process, close, service and liquidate loans;

(2) Has a satisfactory performance history with SBA, including the submission of complete and accurate loan guarantee application packages;

(3) Has an acceptable SBA purchase rate; and

(4) Has shown the ability to work well with the local SBA office.

(b) If the district director does not approve a request for CLP status, the Lender may appeal to the D/FA, whose decision will be final. If SBA grants CLP status, it applies only in the field office that processed the CLP designation. A CLP Lender must execute a Supplemental Guarantee Agreement that will specify a term not to exceed two years.

PREFERRED LENDERS PROGRAM (PLP)

§ 120.450 What is the Preferred Lenders Program?

Under the Preferred Lenders Program (PLP), designated Lenders process, close, service, and liquidate SBA guaranteed loans with reduced requirements for documentation to and prior approval by SBA.

§ 120.451 How does a Lender become a PLP Lender?

(a) An SBA field office serving the area in which a Lender's office is located can nominate the Lender, or a

Lender can request a field office to consider it for PLP status. The SBA field office will forward its recommendation to an SBA centralized loan processing center which will submit its recommendation and supporting documentation to the appropriate Office of Capital Access official in accordance with Delegations of Authority for final decision.

(b) In making its decision, SBA considers whether the Lender:

(1) Has the required ability to process, close, service and liquidate loans;

(2) Has the ability to develop and analyze complete loan packages; and

(3) Has satisfactory SBA performance, as determined by SBA in its discretion. The Lender's Risk Rating, among other factors, will be considered in determining satisfactory SBA performance. Other factors may include, but are not limited to, on-site review/examination assessments, historical performance measures (like default rate, purchase rate and loss rate), loan volume to the extent that it impacts performance measures, and other performance related measurements and information (such as contribution toward SBA mission).

(c) Before it can operate as a PLP Lender, the approved Lender must execute a Supplemental Guarantee Agreement, which will specify a term not to exceed two years.

(d) When a PLP's Supplemental Guarantee Agreement expires, SBA may recertify it as a PLP Lender for an additional term not to exceed two years. Prior to recertification, SBA will review a PLP Lender's loans, policies and procedures. The recertification decision is made by the appropriate Office of Capital Access official in accordance with Delegations of Authority and is final.

(e) When a PLP Lender's Supplemental Guaranty Agreement expires, SBA may recertify the Lender as a PLP Lender for an additional term not to exceed two years. Prior to recertification, SBA will review a PLP Lender's loans, policies, procedures, SBA performance, Risk Rating, review or examination results, and other risk related information as determined by SBA.

Small Business Administration

§ 120.460

(f) A PLP Lender may request an expansion of the territory in which it can process PLP loans by submitting its request to a loan processing center. The center will obtain the recommendation of each SBA office in the area into which the PLP Lender would like to expand its PLP operations. The center will forward the recommendations to the D/FA for final decision. If a PLP Lender is not a CLP Lender in a territory into which it seeks to expand its PLP status, it automatically obtains CLP status in that territory when it is granted PLP status for the territory.

[64 FR 6507-6509, Feb. 10, 1999, as amended at 73 FR 75511, Dec. 11, 2008]

§ 120.452 What are the requirements of PLP loan processing?

(a) Subparts A and B of this part govern the making of PLP loans, except for the following:

(1) Certain types of businesses, loans, and loan programs are not eligible for PLP, as detailed in published SBA policy and procedures.

(2) A Lender may not make a PLP business loan which reduces its existing credit exposure for any Borrower, except in cases where an interim loan(s) has been made for other than real estate construction purposes to the Borrower which was approved by the Lender within 90 days of receipt of the issuance for a subsequent PLP loan number.

(3) SBA will not guarantee more than the specified statutory percentage of any PLP loan.

(b) A PLP Lender notifies SBA of its approval of a PLP loan by submitting to SBA's loan processing center appropriate documentation signed by two of the PLP's authorized representatives. SBA will attach the SBA guarantee and notify the PLP Lender of the SBA loan number (if it does not identify a problem with eligibility, and funds are available).

(c) The PLP Lender is responsible for all PLP loan decisions regarding eligibility (including size) and creditworthiness. The PLP Lender is also responsible for confirming that all PLP loan closing decisions are correct, and that it has complied with all requirements of law and SBA regulations.

§ 120.453 Responsibilities of PLP Lenders for servicing and liquidating 7(a) loans.

Servicing and Liquidation responsibilities for PLP Lenders are set forth in subpart E of this part.

[72 FR 18360, Apr. 12, 2007]

SBA SUPERVISED LENDERS

§ 120.460 What are SBA's additional requirements for SBA Supervised Lenders?

(a) In general. In addition to complying with SBA's requirements for SBA Lenders, an SBA Supervised Lender must meet the additional requirements set forth in this regulation and the SBA Supervised Lender regulations that follow.

(b) Operations and internal controls. Each SBA Supervised Lender's board of directors (or management, if the SBA Supervised Lender is a division of another company and does not have its own board of directors) must adopt an internal control policy which provides adequate direction to the institution in establishing effective control over and accountability for operations, programs, and resources. The internal control policy must, at a minimum:

(1) Direct management to assign responsibility for the internal control function (covering financial, credit, credit review, collateral, and administrative matters) to an officer or officers of the SBA Supervised Lender;

(2) Adopt and set forth procedures for maintenance and periodic review of the internal control function; and

(3) Direct the operation of a program to review and assess the SBA Supervised Lender's assets. The asset review program policies must specify the following:

(i) Loan, loan-related asset, and appraisal review standards, including standards for scope of selection for review (of any such loan, loan-related asset or appraisal) and standards for work papers and supporting documentation;

(ii) Asset quality classification standards consistent with the standardized classification systems used by the Federal Financial Institution Regulators;

§ 120.461

13 CFR Ch. I (1–1–10 Edition)

(iii) Specific internal control requirements for the SBA Supervised Lender's major asset categories (cash and investment securities), lending, and the issuance of debt;

(iv) Specific internal control requirements for the SBA Supervised Lender's oversight of Lender Service Providers; and

(v) Standards for training to implement the asset review program.

[73 FR 75512, Dec. 11, 2008]

§ 120.461 What are SBA's additional requirements for SBA Supervised Lenders concerning records?

(a) *Report filing.* All SBA Supervised Lender-specific reports (including all SBLC-only reports) must be filed with the appropriate Office of Capital Access official in accordance with Delegations of Authority.

(b) *Maintenance of records.* An SBA Supervised Lender must maintain at its principal business office accurate and current financial records, including books of accounts, minutes of stockholder, directors, and executive committee meetings, and all documents and supporting materials relating to the SBA Supervised Lender's transactions. However, securities held by a custodian pursuant to a written agreement are exempt from this requirement.

(c) *Permanent preservation of records.* An SBA Supervised Lender must permanently preserve in a manner permitting immediate (one business day) retrieval the following documentation for the financial statements and other reports required by §120.464 (and the accompanying certified public accountant's opinion):

(1) All general and subsidiary ledgers (or other records) reflecting asset, liability, capital stock and additional paid-in capital, income, and expense accounts;

(2) All general and special journals (or other records forming the basis for entries in such ledgers); and

(3) The corporate charter, bylaws, application for determination of eligibility to participate with SBA, and all minutes books, capital stock certificates or stubs, stock ledgers, and stock transfer registers.

(d) *Other preservation of records.* An SBA Supervised Lender must preserve for at least 6 years following final disposition of each individual SBA loan:

(1) All applications for financing;

(2) Lending, participation, and escrow agreements;

(3) Financing instruments; and

(4) All other documents and supporting material relating to such loans, including correspondence.

(e) *Electronic preservation.* Records and other documents referred to in this section may be preserved electronically if the original is available for retrieval within 15 working days.

[73 FR 75512, Dec. 11, 2008]

§ 120.462 What are SBA's additional requirements on capital maintenance for SBA Supervised Lenders?

(a) *Capital adequacy.* The board of directors (or management, if the SBA Supervised Lender is a division of another company and does not have its own board of directors) of each SBA Supervised Lender must determine capital adequacy goals; that is, the total amount of capital needed to assure the SBA Supervised Lender's continued financial viability and provide for any necessary growth. The minimum standards set in §120.471 for SBLCs and those established by state regulators for NFRLs are not to be adopted as the ideal capital level for a given SBA Supervised Lender. Rather, the minimum standards are to serve as minimum levels of capital that each SBA Supervised Lender must maintain to protect against the credit risk and other general risks inherent in its operation.

(b) *Capital plan.* (1) The board of directors of each SBA Supervised Lender must establish, adopt, and maintain a formal written capital plan. The plan must include any interim capital targets that are necessary to achieve the SBA Supervised Lender's capital adequacy goals as well as the minimum capital standards. The plan must address any projected dividend goals, equity retirements, or any other anticipated action that may decrease the SBA Supervised Lender's capital. The plan must set forth the circumstances

in which capital retirements (e.g., dividends, distributions of capital or purchase of treasury stock) can occur. In addition to factors described above that must be considered in meeting the minimum standards, the board of directors must also address the following factors in developing the SBA Supervised Lender's capital adequacy plan:

- (i) Management capability;
- (ii) Quality of operating policies, procedures, and internal controls;
- (iii) Quality and quantity of earnings;
- (iv) Asset quality and the adequacy of the allowance for loan losses within the loan portfolio;
- (v) Sufficiency of liquidity; and
- (vi) Any other risk-oriented activities or conditions that warrant additional capital (e.g., portfolio growth rate).

(2) An SBA Supervised Lender must keep its capital plan current, updating it at least annually or more often as operating conditions may warrant.

(c) *Certification of compliance.* Within 45 days of the end of each fiscal quarter, each SBA Supervised Lender must furnish the SBA with a calculation of capital and certification of compliance with its minimum capital requirement as set forth in §§ 120.471, 120.472, or 120.474, as applicable, for SBLCs and as established by state regulators for NFRLs. The SBA Supervised Lender's chief financial officer must certify the calculation to be correct. The quarterly calculation and certification of compliance may be included in the SBA Supervised Lender's Quarterly Condition Report.

(d) *Capital impairment.* An SBA Supervised Lender must meet its minimum regulatory capital requirement and avoid capital impairment. Capital impairment exists if an SBA Supervised Lender fails to meet its minimum regulatory capital requirement under §§ 120.471, 120.472, and 120.474 for SBLCs or as established by state regulators for NFRLs. An SBA Supervised Lender must provide the appropriate Office of Capital Access official in accordance with Delegations of Authority written notice of any failure to meet its minimum capital requirement within 30 calendar days of the month-end in which the impairment occurred. Unless

otherwise waived by the appropriate Office of Capital Access official in accordance with Delegations of Authority in writing, an SBA Supervised Lender may not present any loans to SBA for guaranty until the impairment is cured. SBA may waive the presentment prohibition for good cause as determined by SBA in its discretion. In the case of differences in calculating capital or capital requirements between the SBA Supervised Lender and SBA, SBA's calculations will prevail until differences between the two calculations are resolved.

(e) *Capital restoration plan.* (1) *Filing requirement.* An SBA Supervised Lender must file a written capital restoration plan with SBA within 45 days of the date that the SBA Supervised Lender provides notice to SBA under paragraph (d) of this section or receives notice from SBA (whichever is earlier) that the SBA Supervised Lender has not met its minimum capital requirement, unless SBA notifies the SBA Supervised Lender in writing that the plan is to be filed within a different time period.

(2) *Plan content.* An SBA Supervised Lender must detail the steps it will take to meet its minimum capital requirement; the time within which each step will be taken; the timeframe for accomplishing the entire capital restoration; and the person or department at the SBA Supervised Lender charged with carrying out the capital restoration plan.

(3) *SBA response.* SBA will provide written notice of whether the capital restoration plan is approved or not or whether SBA will seek additional information. If the capital restoration plan is not approved by SBA, the SBA Supervised Lender will submit a revised capital restoration plan within the timeframe specified by SBA.

(4) *Amendment of capital restoration plan.* An SBA Supervised Lender that has submitted an approved capital restoration plan may, after prior written notice to and approval by SBA, amend the plan to reflect a change in circumstance. Until such time as a proposed amendment has been approved, the SBA Supervised Lender must implement the capital restoration plan as

§ 120.463

13 CFR Ch. I (1–1–10 Edition)

approved prior to the proposed amendment.

(5) *Failure.* If an SBA Supervised Lender fails to submit a capital restoration plan that is acceptable to SBA within its discretion within the required timeframe, or fails to implement, in any material respect as determined by SBA in its discretion, its SBA approved capital restoration plan within the plan timeframe, SBA may undertake enforcement actions under § 120.1500.

[73 FR 75512, Dec. 11, 2008]

**§ 120.463 Regulatory accounting—
What are SBA's regulatory accounting requirements for SBA Supervised Lenders?**

(a) *Books and records.* The books and records of an SBA Supervised Lender must be kept on an accrual basis in accordance with Generally Accepted Accounting Principles (GAAP) as promulgated by the Financial Accounting Standards Board (FASB), supplemented by Regulatory Accounting Principles (RAP) as identified by SBA in Policy, Procedural or Information Notices, from time to time.

(b) *Annual audit.* Each SBA Supervised Lender must have its financial statements audited annually by a certified public accountant experienced in auditing financial institutions. The audit must be performed in accordance with generally accepted auditing standards as adopted by the Auditing Standards Board of the American Institute of Certified Public Accountants (AICPA) for non-public companies and by the Public Company Accounting Oversight Board (PCAOB) for public companies. Annually, the auditor must issue an audit report with an opinion as to the fairness of the SBA Supervised Lender's financial statements and their compliance with GAAP.

(c) *Auditor qualifications.* The audit shall be conducted by an independent certified public accountant who:

(1) Is registered or licensed to practice as a certified public accountant, and is in good standing, under the laws of the state or other political subdivision of the United States in which the SBA Supervised Lender's principal office is located;

(2) Agrees in the engagement letter with the SBA Supervised Lender to provide the SBA with access to and copies of any work papers, policies, and procedures relating to the services performed;

(3)(i) Is in compliance with the AICPA Code of Professional Conduct; and

(ii) Meets the independence requirements and interpretations of the Securities and Exchange Commission and its staff;

(4) Has received a peer review or is enrolled in a peer review program, that meets AICPA guidelines; and

(5) Is otherwise acceptable to SBA.

(d) *Change of auditor.* If an SBA Supervised Lender discharges or changes its auditor, it must notify SBA in writing within ten days of the occurrence. Such notification must provide:

(1) The name, address, and telephone number of the discharged auditor; and

(2) If the discharge/change involved a dispute over the financial statements, a reasonably detailed statement of all the reasons for the discharge or change. This statement must set out the issue in dispute, the position of the auditor, the position of the SBA Supervised Lender, and the effect of each position on the balance sheet and income statement of the SBA Supervised Lender.

(e) *Specific accounting requirements.* (1) Each SBA Supervised Lender must maintain an allowance for losses on loans and other assets that is sufficient to absorb all probable and estimated losses that may reasonably be expected based on the SBA Supervised Lender's historical performance and reasonably-anticipated events. Each SBA Supervised Lender must maintain documentation of its loan loss allowance calculations and analysis in sufficient detail to permit the SBA to understand the assumptions used and the application of those assumptions to the assets of the SBA Supervised Lender.

(2) The unguaranteed portions of loans determined to be uncollectible must be charged-off promptly. If the portion determined to be uncollectible by the SBA Supervised Lender is different from the amount determined by

Small Business Administration

§ 120.464

its auditors or the SBA, the SBA Supervised Lender must charge-off such amount as the SBA may direct.

(3) Each SBA Supervised Lender must classify loans as:

(i) "Nonaccrual," if any portion of the principal or interest is determined to be uncollectible and

(ii) "Formally restructured," if the loan meets the "troubled debt restructuring" definition set forth in FASB Statement of Financial Accounting Standards No. 15, Accounting by Debtors and Creditors for Troubled Debt Restructurings.

(4) When one loan to a borrower is classified as nonaccrual or formally restructured, all loans to that borrower must be so classified unless the SBA Supervised Lender can document that the loans have independent sources of repayment.

(f) *Valuing loan servicing rights and residual interests.* Each SBA Supervised Lender must account for loan sales transactions and the valuation of loan servicing rights in accordance with GAAP. At the end of each quarter, the SBA Supervised Lender must review for reasonableness the existing environmental assumptions used in the valuation. Particular attention must be given to interest rate and repayment rate assumptions. Assumptions considered no longer reasonable must be modified and modifications must be reflected in the valuation and must be documented and supported by a market analysis. Work papers reflecting the analysis of assumptions and any resulting adjustment in the valuation must be maintained for SBA review in accordance with §120.461. SBA may require an SBA Supervised Lender to use industry averages for the valuation of servicing rights.

[73 FR 75513, Dec. 11, 2008]

§ 120.464 Reports to SBA.

(a) An SBA Supervised Lender must submit the following to SBA:

(1) *Annual Report.* Within three months after the close of each fiscal year, each SBA Supervised Lender must submit to SBA two copies of an annual report including audited financial statements as prepared by a certified public accountant in accordance with §120.463. Specifically, the annual

report must, at a minimum, include the following:

(i) Audited balance sheet;

(ii) Audited statement of income and expense;

(iii) Audited reconciliation of capital accounts;

(iv) Audited source and application of funds;

(v) Such footnotes as are necessary to an understanding of the report;

(vi) Auditor's letter to management on internal control weaknesses; and

(vii) The auditor's report.

(2) *Quarterly Condition Reports.* By the 45th calendar day following the end of each calendar quarter, each SBA Supervised Lender must submit a Quarterly Condition Report in a form and content as the SBA may prescribe from time to time. At a minimum, the Quarterly Condition Report must include the SBA Supervised Lender's quarterly financial statements, which may be internally prepared. The SBA Supervised Lender must apply uniform definitions to categories of nonperforming loans and include recovery amounts on liquidated loans. SBA may, on a case-by-case basis, depending on an SBA Supervised Lender's size and the quality of its assets, adjust the requirements for content and frequency of filing Quarterly Condition Reports.

(3) *Legal and Administrative Proceeding Report.* Each SBA Supervised Lender must report any legal or administrative proceeding by or against the SBA Supervised Lender, or against any officer, director or employee of the SBA Supervised Lender for an alleged breach of official duty, within ten business days after initiating or learning of the proceeding, and also must notify the SBA of the terms of any settlement or final judgment. The SBA Supervised Lender must include such information in any reporting required under other provisions of SBA regulations.

(4) *Stockholder Reports.* Each SBA Supervised Lender must submit to SBA a copy of any report furnished to its stockholders in any manner, within 30 calendar days after submission to stockholders, including any prospectus, letter, or other document, concerning the financial operations or condition of the SBA Supervised Lender.

§ 120.465

13 CFR Ch. I (1–1–10 Edition)

(5) *Reports of Changes.* Each SBA Supervised Lender must submit to SBA a summary of any changes in the SBA Supervised Lender's organization or financing (within 30 calendar days of the change), such as:

(i) Any change in its name, address or telephone number;

(ii) Any change in its charter, by-laws, or its officers or directors (to be accompanied by a statement of personal history on the form approved by SBA);

(iii) Any change in capitalization, including such types of change as are identified in this part 120;

(iv) Any changes affecting an SBA Supervised Lender's eligibility to continue to participate as an SBA Supervised Lender; and

(v) Notice of any pledge of stock (within 30 calendar days of the transaction) if 10 percent or more of the stock is pledged by any person (or group of persons acting in concert) as collateral for indebtedness.

(6) *Report of Changes in Financial Condition.* In addition to other reports required under this part 120, each SBA Supervised Lender must submit a report to SBA on any material change in financial condition. The SBA Supervised Lender must submit such report promptly, but no later than ten days after its management becomes aware of such change (except as provided for in §120.462(d)). Failure to promptly notify SBA concerning a material change in financial condition may lead to enforcement action.

(7) *Other Reports.* Each SBA Supervised Lender must submit such other reports as SBA from time to time may in writing require.

(b) *Preparing financial reports for filing.* Each SBA Supervised Lender must prepare financial reports:

(1) In accordance with all applicable laws, regulations, procedures, standards, and such instructions and specifications and in such form and media format as may be prescribed by SBA from time to time;

(2) On an accrual basis, in accordance with GAAP principles and such other accounting requirements, standards, and procedures as may be prescribed by the SBA from time to time;

(3) That contain all applicable footnotes in accordance with GAAP principles, one of which includes a brief analysis of how the SBA Supervised Lender complies with SBA's capital regulations, as applicable; and

(4) In such manner as to facilitate the reconciliation of these reports with the books and records of the SBA Supervised Lender.

(c) *Responsibility for assuring the accuracy of filed financial reports.* Each financial report filed with SBA must be certified as having been prepared in accordance with all applicable regulations, SOPs, notices, and instructions and to be a true, accurate, and complete representation of the financial condition and financial performance of the SBA Supervised Lender to which it applies. The reports must be certified by the officer of the reporting SBA Supervised Lender named for that purpose by action of the institution's board of directors. If the institution's board of directors has not acted to name an officer to certify the correctness of its reports of financial condition and financial performance, then the reports must be certified by the president or chief executive officer of the reporting SBA Supervised Lender.

(d) *Waiver.* The appropriate Office of Capital Access official in accordance with Delegations of Authority may in his/her discretion waive any §120.464 reporting requirement for SBA Supervised Lenders for good cause (including, but not limited to, where an SBA Supervised Lender has a relatively small SBA loan portfolio), as determined by SBA. SBA Supervised Lenders must request the waiver in writing and include all supporting reasons and documentation. The waiver decision of the appropriate Office of Capital Access official in accordance with Delegations of Authority is final.

[73 FR 75514, Dec. 11, 2008]

§ 120.465 Civil penalty for late submission of required reports.

(a) *Obligation to submit required reports by applicable due dates.* SBA Supervised Lenders must submit complete reports by the due dates described in the regulations or as directed in writing by SBA. SBA considers any report that an SBA Supervised Lender sends to SBA

by the applicable due date but that is submitted only in part, to have not been submitted by the applicable due date. SBA also considers any report that is postmarked by the due date to be submitted by the due date.

(b) *Amount of civil penalty.* For each day past the due date for such report, the SBA Supervised Lender must pay to SBA a civil penalty of not more than \$5,000 per day per report. Such civil penalty continues to accrue until and including the date upon which SBA Supervised Lender submits the complete report. In determining the amount of the civil penalty to be assessed, SBA may consider the financial resources and good faith of the SBA Supervised Lender, the gravity of the violation, the history of previous violations and any such other matters as justice may require.

(c) *Notification of amount of civil penalty.* SBA will notify the SBA Supervised Lender in writing of the amount of civil penalties imposed either upon receiving the required complete report or at such other time as SBA determines. The SBA Supervised Lender must pay this amount to SBA within 30 days of the date of SBA's written demand.

(d) *Identification during examination.* SBA may also impose on an SBA Supervised Lender a civil penalty as described in this section if SBA discovers, during an examination pursuant to subpart I of this Part 120 or otherwise, that the SBA Supervised Lender did not submit a required report by the due date.

(e) *Extensions of submission due dates.* (1) An SBA Supervised Lender may request in writing to SBA that SBA extend its report due date. The request must reference the report and its due date, state the reasonable cause for extension, and assert how much additional time is needed in order to submit a complete report. SBA will advise SBA Supervised Lender in writing as to whether it approved or denied the extension request. If SBA determines that there is reasonable cause to grant an extension and it is not due to willful neglect, SBA will establish a new due date. Such determination as to willful neglect and reasonable cause is in SBA's discretion. SBA will consider the

following factors in determining willful neglect:

(i) Whether the SBA Supervised Lender failed to file required reports for more than two reporting periods and

(ii) If SBA provided the SBA Supervised Lender notice of the failure to file and the SBA Supervised Lender failed to respond or failed to provide a reasonable explanation for the filing failure in its response.

(2) If SBA disapproves the extension, the due date remains the same. The civil penalty accrues regardless of whether the SBA Supervised Lender files an extension request. If SBA approves the extension, SBA will waive the civil penalty that has accrued so far for that particular report. However, a new civil penalty will accrue if the SBA Supervised Lender does not submit a complete report by the new due date established by SBA.

(f) *Requests for reduction or exemption.* (1) An SBA Supervised Lender may request a reduction or exemption from the civil penalty in writing to SBA. The request must reference the required report, its due date and the amount sought for reduction, and state in detail the reasons for the reduction. SBA will consider the following factors:

(i) Whether there is reasonable cause for failure to file timely and it was not due to willful neglect;

(ii) Whether the SBA Supervised Lender has demonstrated to SBA's satisfaction that it has modified its internal procedures to comply with reporting requirements in the future; and

(iii) Whether the SBA Supervised Lender has demonstrated to SBA's satisfaction, based on financial information fully disclosed together with its request, that it would have difficulty paying the civil penalty assessed.

(2) SBA must also determine that a reduction or exemption is not inconsistent with the public interest or the protection of SBA.

(3) SBA may in writing approve the exemption, reduce the civil penalty, or deny the exemption.

(4) If SBA grants the reduction request or denies the reduction or exemption, the SBA Supervised Lender must pay the amount owed within 30 days of

the letter date. Civil penalties will accrue while the request is pending.

(g) *Reconsideration of decisions.* An SBA Supervised Lender may request in writing to the Associate Administrator for Capital Access (AA/CA) to reconsider its request for extension, reduction, or exemption. The reconsideration request must be received by SBA within 30 days of the date of the letter denying the SBA Supervised Lender's original request. SBA will not consider untimely requests. The SBA Supervised Lender must include any additional information or documentation to support its reconsideration request. SBA will issue a written decision on the reconsideration request. The decision is a final agency decision. If on reconsideration, a civil penalty remains due, the SBA Supervised Lender must pay to SBA the civil penalty within 30 days of the written decision or as otherwise directed. Civil penalties will continue to accrue while the reconsideration request is pending.

(h) *Other enforcement actions.* SBA may seek additional remedies for failure to timely file reports as authorized by law.

(i) *Exception for affiliate of SBLC.* Civil penalties under this section do not apply to any affiliate of an SBLC that procures at least 10% of its annual purchasing requirements from small manufacturers.

[73 FR 75515, Dec. 11, 2008]

SMALL BUSINESS LENDING COMPANIES
(SBLC)

§ 120.470 What are SBA's additional requirements for SBLCs?

In addition to complying with SBA's requirements for SBA Lenders and SBA Supervised Lenders, an SBLC must meet the requirements contained in this regulation and the SBLC regulations that follow.

(a) *Lending.* An SBLC may only make:

(1) Loans under section 7(a) (except section 7(a)(13) of the Act in participation with SBA); and/or

(2) SBA guaranteed loans to Intermediaries (see subpart G of this part). Such loans are subject to the same conditions as guaranteed loans made to Intermediaries by 7(a) Lenders.

(b) *Business structure.* An SBLC must be a corporation (profit or non-profit) or a limited liability company or limited partnership.

(c) *Written agreement.* An SBLC must sign a written agreement with SBA.

(d) *Dual control.* An SBLC must maintain dual control over disbursement of funds and withdrawal of securities.

(1) An SBLC may disburse funds only by checks or wire transfers authorized by signatures of two or more officers covered by the SBLC's fidelity bond, except that checks in an amount of \$1,000 or less may be signed by one bonded officer, provided that such action is permitted under the SBLC's fidelity bond.

(2) There must be two or more bonded officers, or one bonded officer and a bonded employee to open safe deposit boxes or withdraw securities from safekeeping. The SBLC must furnish to each depository bank, custodian, or entity providing safe deposit boxes a certified copy of the resolution implementing control procedures.

(e) *Fidelity insurance.* An SBLC must maintain a Brokers Blanket Bond, Standard Form 14, or Finance Companies Blanket Bond, Standard Form 15, or such other form of coverage as SBA may approve, in a minimum amount of \$2,000,000 executed by a surety holding a certificate of authority from the Secretary of the Treasury pursuant to 31 U.S.C. 9304-9308.

(f) *Common control.* (1) An SBLC must not control, be controlled by, or be under common control with another SBLC.

(2) In the case of a purchase of an SBLC by an organization that already owns an SBLC, the purchasing entity will have six months to submit a plan to SBA for the divestiture of one of the SBLCs. All divestiture plans must be approved by SBA and SBA may withhold approval in its discretion. Divestiture of the SBLC must occur within one year of purchase date.

(3) Without prior written SBA approval, an Associate of one SBLC must not be an Associate of another SBLC or of any entity which directly or indirectly controls, or is under common control with, another SBLC.

(4) For purposes of paragraph (f) of this section, common control means a

condition where two or more SBLCs, either through ownership, management, contract, or otherwise, are under the Control of one group or Person (as defined in §120.10 of this chapter). Two or more SBLCs are presumed to be under common control if they are Affiliates of each other by reason of common ownership or common officers, directors, or general partners.

(5) “Affiliate” has the meaning set forth in §121.103 of this chapter.

(6) “Control” means the possession, direct or indirect, of the power to direct or cause the direction of the management and policies of an SBLC or other concern, whether through the ownership of voting securities, by contract, or otherwise. The common control presumption may be rebutted by evidence satisfactory to SBA.

(g) *Management.* An SBLC must employ full time professional management.

(h) *Borrowed funds.* In general, an SBLC may not be capitalized with borrowed funds. Shareholders owning 10 percent or more of any class of its stock must not use personally-borrowed funds to purchase the stock unless the net worth of the shareholder is at least twice the amount borrowed or unless the shareholder receives SBA’s prior written approval for a lower ratio.

[73 FR 75515, Dec. 11, 2008]

§120.471 What are the minimum capital requirements for SBLCs?

(a) *Minimum capital requirements.* Each SBLC must maintain, at a minimum, unencumbered paid-in capital and paid-in surplus of at least \$1,000,000, or ten percent of the aggregate of its share of all outstanding loans, whichever is more.

(b) *Composition of capital.* For purposes of complying with paragraph (a) of this section, capital consists only of one or more of the following:

- (1) Common stock;
- (2) Preferred stock that is noncumulative as to dividends and does not have a maturity date;
- (3) Additional paid-in capital representing amounts paid for stock in excess of the par value;
- (4) Retained earnings of the business; and/or

(5) For limited liability companies and limited partnerships, capital contributions must not be subject to repayment at any specific time, must not be subject to withdrawal and must have no cumulative priority return.

(c) *Voluntary capital reduction.* Without prior written SBA approval, an SBLC must not voluntarily reduce its capital, or repurchase and hold more than 2 percent of any class or combination of classes of its stock.

(d) *Issuance of securities.* Without prior written SBA approval, an SBLC must not issue any securities (including stock options and debt securities) except stock dividends.

[73 FR 75516, Dec. 11, 2008]

§ 120.472 Higher individual minimum capital requirement.

The Associate Administrator for Capital Access (AA/CA) may require, under §120.473(d), an SBLC to maintain a higher level of capital, if the AA/CA determines, in his/her discretion, that the SBLC’s level of capital is potentially inadequate to protect the SBA from loss due to the financial failure of the SBLC. The factors to be considered in the determination will vary in each case and may include, for example:

- (a) Specific conditions or circumstances pertaining to the SBLC;
- (b) Exigency of those circumstances or potential problems;
- (c) Overall condition, management strength, and future prospects of the SBLC and, if applicable, its parent or affiliates;

(d) The SBLC’s liquidity and existing capital level, and the performance of its SBA loan portfolio;

(e) The management views of the SBLC’s directors and senior management; and

(f) Other risk-related factors, as determined by SBA.

[73 FR 75516, Dec. 11, 2008]

§ 120.473 Procedures for determining individual minimum capital requirement.

(a) *Notice.* When SBA determines that an individual minimum capital requirement above that set forth in this subpart or other legal authority is necessary or appropriate for a particular SBLC, SBA will notify the SBLC in

§ 120.474

13 CFR Ch. I (1–1–10 Edition)

writing of the proposed individual minimum capital requirement, the date by which it should be reached and will provide an explanation of why the requirement proposed is considered necessary or appropriate.

(b) *SBLC response.* The SBLC may respond to the notice. The response should include any matters which the SBLC would have SBA consider in deciding whether individual minimum capital requirements should be established for the SBLC, what those capital requirements should be, and, if applicable, when they should be achieved. The response must be in writing and delivered to the AA/CA within 30 days after the date on which the SBLC received the notice. SBA may shorten the time for response when, in the opinion of SBA, the condition of the SBLC so warrants, provided that the SBLC is informed promptly of the new time period, or the SBLC consents to the shortening of its response time. In its discretion, SBA may extend the time period for good cause.

(c) *Failure to respond.* An SBLC that does not respond within 30 days or such other time period as may be specified by SBA will have waived any objections to the proposed minimum capital requirement and the deadline for its achievement. Failure to respond will also constitute consent to the individual minimum capital requirement.

(d) *Decision.* After the close of the SBLC's response period, the AA/CA will decide, based on a review of SBA reasons for proposing the individual minimum capital requirement, the SBLC's response, and other information concerning the SBLC, whether the individual minimum capital requirement should be established for the SBLC and, if so, the requirement and the date it will become effective. The SBLC will be notified of the decision in writing. The notice will include an explanation of the decision; except for a decision not to establish an individual minimum capital requirement for the SBLC.

(e) *Submission of plan.* The decision may require the SBLC to develop and submit to SBA, within a time period specified, an acceptable plan to reach the individual minimum capital requirement by the date required.

(f) *Change in circumstances.* If, after SBA's decision in paragraph (d) of this section, there is a change in the circumstances affecting the SBLC's capital adequacy or its ability to reach the required individual minimum capital requirement by the specified date, either the SBLC or the AA/CA may propose to the other a change in the individual minimum capital requirement for the SBLC, the date when the individual minimum must be achieved, and/or the SBLC's plan (if applicable). The AA/CA may decline to consider proposals that are not based on a significant change in circumstances or are repetitive or frivolous. Pending a decision by the AA/CA on reconsideration, SBA's original decision and any plan required under that decision will continue in full force and effect.

[73 FR 75516, Dec. 11, 2008]

§ 120.474 Relation to other actions.

In lieu of, or in addition to, the procedures in this subpart, the individual minimum capital requirement for an SBLC may be established or revised through a written agreement or cease and desist proceedings under subpart I of this part.

[73 FR 75517, Dec. 11, 2008]

§ 120.475 Change of ownership or control.

(a) Any change of ownership or control without prior written approval of SBA is prohibited. An SBLC must request approval of any such change from the appropriate Office of Capital Access official in accordance with Delegations of Authority. Pending the approval, the SBLC may not register the proposed new owners on its transfer books nor permit them to participate in any manner in the conduct of the SBLC's affairs. Change of ownership or control includes:

(1) Any transfer of 10 percent or more of any class of the SBLC's stock, and any agreement providing for such transfer;

(2) Any transfer that could result in the beneficial ownership by any person or group of persons acting in concert of 10 percent or more of any class of its stock, and any agreement providing for such transfer;

Small Business Administration

§ 120.520

(3) Any merger, consolidation, or reorganization; or

(4) Any other transaction or agreement that transfers control of the SBLC.

(b) If transfer of ownership or control is subject to the approval of any State or Federal chartering, licensing, or other regulatory authority, copies of any documents filed with such authority must, at the same time, be transmitted to the appropriate Office of Capital Access official in accordance with Delegations of Authority.

[61 FR 3235, Jan. 31, 1996. Redesignated and amended at 73 FR 75516, Dec. 11, 2008]

§ 120.476 Prohibited financing.

An SBLC may not make a loan to a small business that has received financing (or a commitment for financing) from an SBIC that is an Associate of the SBLC.

[61 FR 3235, Jan. 31, 1996. Redesignated at 73 FR 75516, Dec. 11, 2008]

§ 120.490 Audits.

Every SBLC is subject to periodic audits by SBA's Office of Inspector General, Auditing Division, and the cost of such audits will be assessed against the SBLC, except for the first audit. Fees are structured based on the SBLC's assets as of the date of the latest audited financial statement submitted to SBA before the audit. The fee schedule is set forth in SBA's Standard Operating Procedures manual.

[61 FR 3235, Jan. 31, 1996. Redesignated at 73 FR 75516, Dec. 11, 2008]

Subpart E—Servicing, Liquidation and Debt Collection Litigation of 7(a) and 504 Loans

SBA'S PURCHASE OF A GUARANTEED PORTION

§ 120.520 Purchase of 7(a) loan guarantees.

(a) *When SBA will purchase*—(1) *For loans approved on or after May 14, 2007.* A Lender may demand in writing that SBA honor its guarantee if the Borrower is in default on any installment for more than 60 calendar days (or less if SBA agrees) and the default has not been cured, provided all business per-

sonal property securing the defaulted SBA loan has been liquidated. A Lender may also submit a request for purchase of a defaulted 7(a) loan when a Borrower files for federal bankruptcy once a period of at least 60 days has elapsed since the last full installment payment. If a Borrower cures a default before a Lender requests purchase by SBA, the Lender's right to request purchase on that default lapses. SBA considers liquidation of business personal property collateral to be completed when a Lender has exhausted all prudent and commercially reasonable efforts to collect upon these assets. In addition, SBA, in its sole discretion, may purchase the guaranteed portion of a loan at any time whether in default or not, with or without the request from a Lender.

(2) *For loans approved before May 14, 2007.* The regulations applicable to the time that a Lender may make demand for purchase that were in effect immediately prior to this date will govern such loans.

(b) *Documentation for purchase.* SBA will not purchase its guaranteed portion of a loan from a Lender unless the Lender has submitted to SBA documentation that SBA deems sufficient to allow SBA to determine whether purchase of the guarantee is warranted under § 120.524.

(c) *Purchase of loans sold in Secondary Market.* When the Lender has sold the guaranteed portion of a loan in the Secondary Market, under subpart F of this part, Lenders must perform all necessary servicing and liquidation actions for such loan even after SBA has purchased the guaranteed portion of such loan from a Registered Holder (as that term is defined in § 120.600(i)). In the event that SBA purchases its guaranteed portion of such a loan from the Registered Holder, Lenders must provide SBA with a loan status report within 15 business days of such purchase. This report should include but not be limited to, a status report on the borrower and current condition of the collateral, plans for any type of loan workout or loan restructuring, existing liquidation activities including the sale of loan collateral, or the status of ongoing foreclosure proceedings.