required with each request for payment. Grantees will be required to submit audited financial statements on an annual basis, if available, or annual financial statements prepared by a licensed, independent public accountant, within 120 calendar days of the end of the grantee's fiscal year.

(2) For recipients of Research and Development Grants, reports will be required in accordance with agreed upon milestones and as part of the disbursement process.

(3) For recipients of Discretionary Grants, reports will be required as appropriate for the project, or on a schedule as described in paragraph (a)(1) of this section, whichever is more frequent.

(b) In addition, SBA may, from time to time, make site visits to the grantee, and review all applicable books and records.

§ 119.18 What are the restrictions against lobbying?

No assistance made available under the PRIME program may be expended by a grantee or subgrantee to pay any person to influence, or attempt to influence, any agency, elected official, officer, or employee of a Federal, State, or local government in connection with its participation in the program.

§ 119.19 Is fundraising an allowable expense under the PRIME program?

Expenditures of grant funds for fundraising activities are not allowable costs under this program. Applicants must be able to raise matching funds without the assistance of grant funds. Unless the full requirement for matching funds is waived, the applicant must demonstrate that it has adequate fundraising resources to obtain the required non-Federal matching funds to perform the project.

§ 119.20 Should grantees and subgrantees raise conflict of interest matters with SBA?

Each grantee or subgrantee must provide SBA with a copy of its conflicts of interest policies prior to receipt of funding under the program. Such policies must clearly describe the grantee's or subgrantee's protections from conflicts of interest or the appearance thereof in the handling of grant funding and program provision under this program.

PART 120—BUSINESS LOANS

GENERAL DESCRIPTIONS OF SBA'S BUSINESS LOAN PROGRAMS

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REQUIREMENTS IMPOSED UNDER OTHER LAWS AND ORDERS

AUTHORITY: 15 U.S.C. 634(b) (6), (b) (7), (b) (14), (h), and note, 636(a), (h) and (m), 650, 687(f), 696(3) and (7), and 697(a) and (e); Pub. L. 111–5, 123 Stat. 115, Pub. L. 111–240, 124 Stat. 2504.

SOURCE: 61 FR 3235, Jan. 31, 1996, unless otherwise noted.

EDITORIAL NOTE: Nomenclature changes to part 120 appear at 72 FR 50039, Aug. 30, 2007.

GENERAL DESCRIPTIONS OF SBA'S BUSINESS LOAN PROGRAMS

§ 120.1 Which loan programs does this part cover?

This part regulates SBA's financial assistance to small businesses under its general business loan programs (''7(a) loans'') authorized by section 7(a) of the Small Business Act (''the Act''), 15 U.S.C. 636(a), its microloan demonstration loan program (''Microloans'') authorized by section 7(m) of the Act, 15 U.S.C. 636(m), and its development company program (''504 loans'') authorized by Title V of the Small Business Investment Act, 15 U.S.C. 695 to 697f (''Title V''). These three programs constitute the business loan programs of the SBA.

§ 120.2 Descriptions of the business loan programs.

(a) *7(a) loans.* (1) 7(a) loans provide financing for general business purposes and may be:

(i) A direct loan by SBA;

(ii) An immediate participation loan by a Lender and SBA; or

(iii) A guaranteed loan (deferred participation) by which SBA guarantees a portion of a loan made by a Lender.

(2) A guaranteed loan is initiated by a Lender agreeing to make an SBA guaranteed loan to a small business and applying to SBA for SBA's guarantee under a blanket guarantee agreement (participation agreement) between SBA and the Lender. If SBA agrees to guarantee (authorizes) a portion of the loan, the Lender funds and services the loan. If the small business defaults on the loan, SBA's guarantee requires SBA to purchase its portion of the outstanding balance, upon demand by the Lender and subject to specific conditions. Regulations specific to 7(a) loans are found in subpart B of this part.

(b) *Microloans.* SBA makes loans and loan guarantees to non-profit Intermediaries that make short-term loans up to $50,000 to eligible small businesses for general business purposes, except payment of personal debts. SBA also makes grants to Intermediaries for use in providing management assistance and counseling to small businesses. Regulations specific to these loans are found in subpart G of this part.

(c) *504 loans.* Projects involving 504 loans require long-term fixed-asset financing for small businesses. A Certified Development Company (CDC) provides the final portion of this financing with a 504 loan made from the proceeds of a Debenture issued by the CDC, guaranteed 100 percent by SBA (with the full faith and credit of the United States), and sold to investors. The regulations specific to these loans are found in subpart H of this part.

[61 FR 3235, Jan. 31, 1996, as amended at 76 FR 63545, Oct. 12, 2011]

§ 120.3 Pilot programs.

The Administrator of SBA may from time to time suspend, modify, or waive rules for a limited period of time to test new programs or ideas. The Administrator shall publish a document in the FEDERAL REGISTER explaining the reasons for these actions.

DEFINITIONS

§ 120.10 Definitions.

The following terms have the same meaning wherever they are used in this part. Defined terms are capitalized wherever they appear.

Acceptable Risk Rating is an SBA-assigned Risk Rating, currently defined by SBA as ''1'', ''2'' or ''3'' on a scale of 1 to 5, which represents an acceptable level of risk as determined by SBA, and which may be revised by SBA from time to time as published in the FEDERAL REGISTER through notice and comment.

Associate. (1) An Associate of a Lender or CDC is:

(i) An officer, director, key employee, or holder of 20 percent or more of the value of the Lender's or CDC's stock or debt instruments, or an agent involved in the loan process;

(ii) Any entity in which one or more individuals referred to in paragraphs (1)(i) of this definition or a Close Relative of any such individual owns or controls at least 20 percent.

(2) An Associate of a small business is:

(i) An officer, director, owner of more than 20 percent of the equity, or key employee of the small business;

(ii) Any entity in which one or more individuals referred to in paragraphs (2)(i) of this definition owns or controls at least 20 percent; and

(iii) Any individual or entity in control of or controlled by the small business (except a Small Business Investment Company (''SBIC'') licensed by SBA).

(3) For purposes of this definition, the time during which an Associate relationship exists commences six months before the following dates and continues as long as the certification, participation agreement, or loan is outstanding:

(i) For a CDC, the date of certification by SBA;

(ii) For a Lender, the date of application for a loan guarantee on behalf of an applicant; or

(iii) For a small business, the date of the loan application to SBA, the CDC, the Intermediary, or the Lender.

Authorization is SBA's written agreement providing the terms and conditions under which SBA will make or guarantee business loans. It is not a contract to make a loan.

Authorized CDC Liquidator is a CDC in good standing with authority under the Act and SBA regulations to conduct liquidation and certain debt collection litigation in connection with 504 loans, as authorized by § 120.975.

Borrower is the obligor of an SBA business loan.

Certified Development Company (''CDC'') is an entity authorized by SBA to deliver 504 financing to small businesses.

Close Relative is a spouse; a parent; or a child or sibling, or the spouse of any such person.

Eligible Passive Company is a small entity or trust which does not engage in regular and continuous business activity, which leases real or personal property to an Operating Company for use in the Operating Company's business, and which complies with the conditions set forth in § 120.111.

Federal Financial Institution Regulator is the federal banking regulator of a 7(a) Lender and may include the Federal Deposit Insurance Corporation, the Federal Reserve Board, the Office of the Comptroller of the Currency, the Office of Thrift Supervision, the National Credit Union Administration, and the Farm Credit Administration.

Intermediary is the entity in the Microloan program that receives SBA financial assistance and makes loans to small businesses in amounts up to $50,000.

Lender or 7(a) Lender is an institution that has executed a participation agreement with SBA under the guaranteed loan program.

Lender Oversight Committee is a committee within SBA, with responsibilities as outlined in Delegations of Authority, as published in the FEDERAL REGISTER.

Less Than Acceptable Risk Rating is an SBA-assigned Risk Rating, currently defined by SBA as ''4'' or ''5'' on a scale of 1 to 5, which represents a higher level of risk as determined by SBA, and which may be revised by SBA from time to time as published in the FEDERAL REGISTER through notice and comment.

Loan Instruments are the Authorization, note, instruments of hypothecation, and all other agreements and documents related to a loan.

Loan program requirements are requirements imposed upon Lenders or CDCs by statute, SBA regulations, any agreement the Lender or CDC has executed with SBA, SBA SOPs, official SBA notices and forms applicable to the 7(a) and 504 loan programs, and loan authorizations, as such requirements are issued and revised by SBA from time to time. For CDCs, this term also includes requirements imposed by Debentures, as that term is defined in § 120.802.

Management Official is an officer, director, general partner, manager, employee participating in management, agent or other participant in the management of the affairs of the SBA Supervised Lender's activities under the 7(a) program.

Non-Federally Regulated Lender (NFRL) is a business concern that is authorized by the SBA to make loans under section 7(a) and is subject to regulation by a state but whose lending activities are not regulated by a Federal Financial Institution Regulator.

Operating Company is an eligible small business actively involved in conducting business operations now or about to be located on real property owned by an Eligible Passive Company, or using or about to use in its business operations personal property owned by an Eligible Passive Company.

Other Regulated SBLC is a Small Business Lending Company whose SBA operations receive regular safety and soundness examinations by a state banking regulator or a Federal Financial Institution Regulator, and which meets the requirements set forth in § 120.1511.

Person is any individual, corporation, partnership, association, unit of government, or legal entity, however organized.

Preference is any arrangement giving a Lender or a CDC a preferred position compared to SBA relating to the making, servicing, or liquidation of a business loan with respect to such things as repayment, collateral, guarantees, control, maintenance of a compensating balance, purchase of a Certificate of deposit or acceptance of a separate or companion loan, without SBA's consent.

Rentable Property is the total square footage of all buildings or facilities used for business operations.

Risk Rating is an SBA internal composite rating assigned to individual SBA Lenders, Intermediaries, or NTAPs that reflects the risk associated with the SBA Lender's or Intermediary's portfolio of SBA loans or with the NTAP. Risk Ratings currently range from one to five, with one representing the least risk and five representing the most risk, and may be revised by SBA from time to time as published in the FEDERAL REGISTER through notice and comment.

Rural Area is a political subdivision or unincorporated area in a non-metropolitan county (as defined by the Department of Agriculture), or, if in a metropolitan county, any such subdivision or area with a resident population under 20,000 which is designated by SBA as rural.

SBA Lender is a 7(a) Lender or a CDC. This term includes SBA Supervised Lenders.

SBA Supervised Lender is a 7(a) Lender that is either a Small Business Lending Company or a NFRL.

Service Provider is an entity that contracts with a Lender or CDC to perform management, marketing, legal or other services.

Small Business Lending Company (SBLC) is a nondepository lending institution that is SBA licensed and is authorized by SBA to only make loans pursuant to section 7(a) of the Small Business Act and loans to Intermediaries in SBA's Microloan program. SBA has imposed a moratorium on licensing new SBLCs since January 1982.

SOPs are SBA Standard Operating Procedures, as issued and revised by SBA from time to time. SOPs are publicly available on SBA's Web site at *http://www.sba.gov* in the online library.

[61 FR 3235, Jan. 31, 1996, as amended at 64 FR 2117, Jan. 13, 1999; 68 FR 57980, Oct. 7, 2003; 72 FR 18360, Apr. 12, 2007; 73 FR 75510, Dec. 11, 2008; 76 FR 63545, Oct. 12, 2011]

Subpart A—Policies Applying to All Business Loans

ELIGIBILITY REQUIREMENTS

§ 120.100 What are the basic eligibility requirements for all applicants for SBA business loans?

To be eligible for an SBA business loan, a small business applicant must:

(a) Be an operating business (except for loans to Eligible Passive Companies);

(b) Be organized for profit;

(c) Be located in the United States;

(d) Be small under the size requirements of part 121 of this chapter (including affiliates). See subpart H of this part for the size standards of part 121 of this chapter which apply only to 504 loans; and

(e) Be able to demonstrate a need for the desired credit.

§ 120.101 Credit not available elsewhere.

SBA provides business loan assistance only to applicants for whom the desired credit is not otherwise available on reasonable terms from non-Federal sources. SBA requires the Lender or CDC to certify or otherwise show that the desired credit is unavailable to the applicant on reasonable terms and conditions from non-Federal sources without SBA assistance, taking into consideration the prevailing rates and terms in the community in or near where the applicant conducts business, for similar purposes and periods of time. Submission of an application to SBA by a Lender or CDC constitutes certification by the Lender or CDC that it has examined the availability of credit to the applicant, has based its certification upon that examination, and has substantiation in its file to support the certification.

§ 120.103 Are farm enterprises eligible?

Federal financial assistance to agricultural enterprises is generally made

by the United States Department of Agriculture (USDA), but may be made by SBA under the terms of a Memorandum of Understanding between SBA and USDA. Farm-related businesses which are not agricultural enterprises are eligible businesses under SBA's business loan programs.

§ 120.104 Are businesses financed by SBICs eligible?

SBA may make or guarantee loans to a business financed by an SBIC if SBA's collateral position will be superior to that of the SBIC. SBA may also make or guarantee a loan to an otherwise eligible small business which temporarily is owned or controlled by an SBIC under the regulations in part 107 of this chapter. SBA neither guarantees SBIC loans nor makes loans jointly with SBICs.

§ 120.105 Special consideration for veterans.

SBA will give special consideration to a small business owned by a veteran or, if the veteran chooses not to apply, to a business owned or controlled by one of the veteran's dependents. If the veteran is deceased or permanently disabled, SBA will give special consideration to one survivor or dependent. SBA will process the application of a business owned or controlled by a veteran or dependent promptly, resolve close questions in the applicant's favor, and pay particular attention to maximum loan maturity. For SBA loans, a veteran is a person honorably discharged from active military service.

INELIGIBLE BUSINESSES AND ELIGIBLE PASSIVE COMPANIES

§ 120.110 What businesses are ineligible for SBA business loans?

The following types of businesses are ineligible:

(a) Non-profit businesses (for-profit subsidiaries are eligible);

(b) Financial businesses primarily engaged in the business of lending, such as banks, finance companies, and factors (pawn shops, although engaged in lending, may qualify in some circumstances);

(c) Passive businesses owned by developers and landlords that do not actively use or occupy the assets acquired or improved with the loan proceeds (except Eligible Passive Companies under § 120.111);

(d) Life insurance companies;

(e) Businesses located in a foreign country (businesses in the U.S. owned by aliens may qualify);

(f) Pyramid sale distribution plans;

(g) Businesses deriving more than one-third of gross annual revenue from legal gambling activities;

(h) Businesses engaged in any illegal activity;

(i) Private clubs and businesses which limit the number of memberships for reasons other than capacity;

(j) Government-owned entities (except for businesses owned or controlled by a Native American tribe);

(k) Businesses principally engaged in teaching, instructing, counseling or indoctrinating religion or religious beliefs, whether in a religious or secular setting;

(l) [Reserved]

(m) Loan packagers earning more than one third of their gross annual revenue from packaging SBA loans;

(n) Businesses with an Associate who is incarcerated, on probation, on parole, or has been indicted for a felony or a crime of moral turpitude;

(o) Businesses in which the Lender or CDC, or any of its Associates owns an equity interest;

(p) Businesses which:

(1) Present live performances of a prurient sexual nature; or

(2) Derive directly or indirectly more than *de minimis* gross revenue through the sale of products or services, or the presentation of any depictions or displays, of a prurient sexual nature;

(q) Unless waived by SBA for good cause, businesses that have previously defaulted on a Federal loan or Federally assisted financing, resulting in the Federal government or any of its agencies or Departments sustaining a loss in any of its programs, and businesses owned or controlled by an applicant or any of its Associates which previously owned, operated, or controlled a business which defaulted on a Federal loan (or guaranteed a loan which was defaulted) and caused the Federal government or any of its agencies or Departments to sustain a loss in any of its

programs. For purposes of this section, a compromise agreement shall also be considered a loss;

(r) Businesses primarily engaged in political or lobbying activities; and

(s) Speculative businesses (such as oil wildcatting).

[61 FR 3235, Jan. 31, 1996, as amended at 82 FR 39502, Aug. 21, 2017]

§ 120.111 What conditions must an Eligible Passive Company satisfy?

An Eligible Passive Company must use loan proceeds only to acquire or lease, and/or improve or renovate, real or personal property (including eligible refinancing), that it leases to one or more Operating Companies for conducting the Operating Company's business, or to finance a change of ownership between the existing owners of the Eligible Passive Company. When the Operating Company is a co-borrower on the loan, loan proceeds also may be used by the Operating Company for working capital and/or the purchase of other assets, including intangible assets, for the Operating Company's use as provided in paragraph (a)(5) of this section. (References to Operating Company in paragraphs (a) and (b) of this section mean each Operating Company.) In the 504 loan program, if the Eligible Passive Company owns assets in addition to the real estate or other eligible long-term fixed assets, loan proceeds may not be used to finance a change of ownership between existing owners of the Eligible Passive Company unless the additional assets owned by the Eligible Passive Company are directly related to the real estate or other eligible long-term fixed assets, the amount attributable to the additional assets is de minimis, and the additional assets are excluded from the Project financing. Any ownership structure or legal form may qualify as an Eligible Passive Company. Any ownership structure or legal form may qualify as an Eligible Passive Company.

(a) Conditions that apply to all legal forms:

(1) The Operating Company must be an eligible small business, and the proposed use of the proceeds must be an eligible use if the Operating Company were obtaining the financing directly;

(2) The Eligible Passive Company (with the exception of a trust) and the Operating Company each must be small under the appropriate size standards in part 121 of this chapter;

(3) The lease between the Eligible Passive Company and the Operating Company must be in writing and must be subordinate to SBA's mortgage, trust deed lien, or security interest on the property. The Eligible Passive Company (as landlord) must furnish as collateral for the loan an assignment of all rents paid under the lease. The rent or lease payments cannot exceed the amount necessary to make the loan payment to the lender, and an additional amount to cover the Eligible Passive Company's direct expenses of holding the property, such as maintenance, insurance and property taxes;

(4) The lease between the Eligible Passive Company and the Operating Company, including options to renew exercisable solely by the Operating Company, must have a remaining term at least equal to the term of the loan;

(5) The Operating Company must be a guarantor or co-borrower with the Eligible Passive Company. In a 7(a) loan that includes working capital and/or the purchase of other assets, including intangible assets, for the Operating Company's use, the Operating Company must be a co-borrower.

(6) Each holder of an ownership interest constituting at least 20 percent of either the Eligible Passive Company or the Operating Company must guarantee the loan. The trustee shall execute the guaranty on behalf of any trust. When deemed necessary for credit or other reasons, SBA or, for a loan processed under an SBA Lender's delegated authority, the SBA Lender may require other appropriate individuals or entities to provide full or limited guarantees of the loan without regard to the percentage of their ownership interests, if any.

(b) *Additional conditions that apply to trusts.* The eligibility status of the trustor will determine trust eligibility. All donors to the trust will be deemed to have trustor status for eligibility purposes. A trust qualifying as an Eligible Passive Company may engage in other activities as authorized by its trust agreement. The trustee must

warrant and certify that the trust will not be revoked or substantially amended for the term of the loan without the consent of SBA. The trustor must guarantee the loan. For purposes of this section, the trustee shall certify to SBA that:

(1) The trustee has authority to act;

(2) The trust has the authority to borrow funds, pledge trust assets, and lease the property to the Operating Company;

(3) The trustee has provided accurate, pertinent language from the trust agreement confirming the above; and

(4) The trustee has provided and will continue to provide SBA with a true and complete list of all trustors and donors.

[61 FR 3235, Jan. 31, 1996; 61 FR 7986, Mar. 1, 1996, as amended at 64 FR 2117, Jan. 13, 1999; 77 FR 19533, Apr. 2, 2012; 82 FR 39502, Aug. 21, 2017]

USES OF PROCEEDS

§ 120.120 What are eligible uses of proceeds?

A small business must use an SBA business loan for sound business purposes. The uses of proceeds are prescribed in each loan's Authorization.

(a) A Borrower may use loan proceeds from any SBA loan to:

(1) Acquire land (by purchase or lease);

(2) Improve a site (e.g., grading, streets, parking lots, landscaping), including up to 5 percent for community improvements such as curbs and sidewalks;

(3) Purchase one or more existing buildings;

(4) Convert, expand or renovate one or more existing buildings;

(5) Construct one or more new buildings; and/or

(6) Acquire (by purchase or lease) and install fixed assets (for a 504 loan, these assets must have a useful life of at least 10 years and be at a fixed location, although short-term financing for equipment, furniture, and furnishings may be permitted where essential to and a minor portion of the 504 Project).

(b) A Borrower may also use 7(a) and microloan proceeds for:

(1) Inventory;

(2) Supplies;

(3) Raw materials; and

(4) Working capital (if the Operating Company is a co-borrower with the Eligible Passive Company, part of the loan proceeds may be applied for working capital and/or the purchase of other assets, including intangible assets, for use by the Operating Company).

(c) A Borrower may use 7(a) loan proceeds for refinancing certain outstanding debts.

[61 FR 3235, Jan. 31, 1996, as amended at 77 FR 19533, Apr. 2, 2012]

§ 120.130 Restrictions on uses of proceeds.

SBA will not authorize nor may a Borrower use loan proceeds for the following purposes (including the replacement of funds used for any such purpose):

(a) Payments, distributions or loans to Associates of the applicant (except for ordinary compensation for services rendered);

(b) Refinancing a debt owed to a Small Business Investment Company (''SBIC'') or a New Markets Venture Capital Company (''NMVCC'');

(c) Floor plan financing or other revolving line of credit, except under § 120.340 or § 120.390;

(d) Investments in real or personal property acquired and held primarily for sale, lease, or investment (except for a loan to an Eligible Passive Company or to a small contractor under § 120.310);

(e) The applicant may not use any of the proceeds to pay past-due Federal, state, or local payroll taxes, sales taxes, or other similar taxes that are required to be collected by the applicant and held in trust on behalf of a Federal, state, or local government entity.

(f) A purpose which does not benefit the small business; or

(g) Any use restricted by §§ 120.201, 120.202, and 120.884 (specific to 7(a) loans and 504 loans respectively).

[61 FR 3235, Jan. 31, 1996, as amended at 76 FR 9218, Feb. 17, 2011; 76 FR 63545, Oct. 12, 2011; 82 FR 39502, Aug. 21, 2017]

§ 120.131 Leasing part of new construction or existing building to another business.

(a) If the SBA financing (whether 7(a) or 504) is for the construction of a new building, a Borrower may permanently lease up to 20 percent of the Rentable Property to one or more tenants if the Borrower permanently occupies and uses no less than 60 percent of the Rentable Property, and plans to permanently occupy and use within three years some of the remaining space not immediately occupied and not permanently leased and plans to permanently occupy and use within ten years all of the remaining space not permanently leased. If the Borrower is an Eligible Passive Company which leases 100 percent of the new building's space to one or more Operating Companies, the Operating Company, or Operating Companies together, must follow the same rules set forth in this paragraph.

(b) If the SBA financing (whether 7(a) or 504) is for the acquisition, renovation, or reconstruction of an existing building, the Borrower may permanently lease up to 49 percent of the Rentable Property if the Borrower permanently occupies and uses no less than 51 percent of the Rentable Property. If the Borrower is an Eligible Passive Company which leases 100 percent of the space of the existing building to one or more Operating Companies, the Operating Company, or Operating Companies together, must follow the same rules set forth in this paragraph.

[68 FR 51679, Aug. 28, 2003]

ETHICAL REQUIREMENTS

§ 120.140 What ethical requirements apply to participants?

Lenders, Intermediaries, and CDCs (in this section, collectively referred to as ''Participants''), must act ethically and exhibit good character. Ethical indiscretion of an Associate of a Participant or a member of a CDC will be attributed to the Participant. A Participant must promptly notify SBA if it obtains information concerning the unethical behavior of an Associate. The following are examples of such unethical behavior. A Participant may not:

(a) Self-deal;

(b) Have a real or apparent conflict of interest with a small business with which it is dealing (including any of its Associates or an Associate's Close Relatives) or SBA;

(c) Own an equity interest in a business that has received or is applying to receive SBA financing (during the term of the loan or within 6 months prior to the loan application);

(d) Be incarcerated, on parole, or on probation;

(e) Knowingly misrepresent or make a false statement to SBA;

(f) Engage in conduct reflecting a lack of business integrity or honesty;

(g) Be a convicted felon, or have an adverse final civil judgment (in a case involving fraud, breach of trust, or other conduct) that would cause the public to question the Participant's business integrity, taking into consideration such factors as the magnitude, repetition, harm caused, and remoteness in time of the activity or activities in question;

(h) Accept funding from any source that restricts, prioritizes, or conditions the types of small businesses that the Participant may assist under an SBA program or that imposes any conditions or requirements upon recipients of SBA assistance inconsistent with SBA's loan programs or regulations;

(i) Fail to disclose to SBA all relationships between the small business and its Associates (including Close Relatives of Associates), the Participant, and/or the lenders financing the Project of which it is aware or should be aware;

(j) Fail to disclose to SBA whether the loan will:

(1) Reduce the exposure of a Participant or an Associate of a Participant in a position to sustain a loss;

(2) Directly or indirectly finance the purchase of real estate, personal property or services (including insurance) from the Participant or an Associate of the Participant;

(3) Repay or refinance a debt due a Participant or an Associate of a Participant; or

(4) Require the small business, or an Associate (including Close Relatives of Associates), to invest in the Participant (except for institutions which require an investment from all members

as a condition of membership, such as a Production Credit Association);

(k) Issue a real estate forward commitment to a builder or developer; or

(l) Engage in any activity which taints its objective judgment in evaluating the loan.

[61 FR 3235, Jan. 31, 1996, as amended at 68 FR 57980, Oct. 7, 2003]

CREDIT CRITERIA FOR SBA LOANS

§ 120.150 What are SBA's lending criteria?

The applicant (including an Operating Company) must be creditworthy. Loans must be so sound as to reasonably assure repayment. SBA will consider:

(a) Character, reputation, and credit history of the applicant (and the Operating Company, if applicable), its Associates, and guarantors;

(b) Experience and depth of management;

(c) Strength of the business;

(d) Past earnings, projected cash flow, and future prospects;

(e) Ability to repay the loan with earnings from the business;

(f) Sufficient invested equity to operate on a sound financial basis;

(g) Potential for long-term success;

(h) Nature and value of collateral (although inadequate collateral will not be the sole reason for denial of a loan request); and

(i) The effect any affiliates (as defined in part 121 of this chapter) may have on the ultimate repayment ability of the applicant.

§ 120.151 What is the statutory limit for total loans to a Borrower?

The aggregate amount of the SBA portions of all loans to a single Borrower, including the Borrower's affiliates as defined in §121.301(f) of this chapter, must not exceed a guaranty amount of $3,750,000, except as otherwise authorized by statute for a specific program. The maximum loan amount for any one 7(a) loan is $5,000,000. The amount of any loan received by an Eligible Passive Company applies to the loan limit of both the Eligible Passive Company and the Operating Company.

[61 FR 3235, Jan. 31, 1996, as amended at 68 FR 51680, Aug. 28, 2003; 76 FR 63546, Oct. 12, 2011; 81 FR 41428, June 27, 2016]

§ 120.160 Loan conditions.

The following requirements are normally required by SBA for all business loans:

(a) *Personal guarantees.* Holders of at least a 20 percent ownership interest generally must guarantee the loan. When deemed necessary for credit or other reasons, SBA or, for a loan processed under an SBA Lender's delegated authority, the SBA Lender, may require other appropriate individuals or entities to provide full or limited guarantees of the loan without regard to the percentage of their ownership interests, if any.

(b) *Appraisals.* SBA may require professional appraisals of the applicant's and principals' assets, a survey, or a feasibility study.

(c) *Hazard Insurance.* SBA requires hazard insurance on all collateral.

[61 FR 3235, Jan. 31, 1996, as amended at 82 FR 39502, Aug. 21, 2017]

REQUIREMENTS IMPOSED UNDER OTHER LAWS AND ORDERS

§ 120.170 Flood insurance.

Under the Flood Disaster Protection Act of 1973 (Sec. 205(b) of Pub. L. 93–234; 87 Stat. 983 (42 U.S.C. 4000 *et seq.*)), a loan recipient must obtain flood insurance if any building (including mobile homes), machinery, or equipment acquired, installed, improved, constructed, or renovated with the proceeds of SBA financial assistance is located in a special flood hazard area. The requirement applies also to any inventory (business loan program), fixtures or furnishings contained or to be contained in the building. Mobile homes on a foundation are buildings. SBA, Lenders, CDCs, and Intermediaries must notify Borrowers that flood insurance must be maintained.

§ 120.171 Compliance with child support obligations.

Any holder of 50% or more of the ownership interest in the recipient of an SBA loan must certify that he or

she is not more than 60 days delinquent on any obligation to pay child support arising under:

(a) An administrative order;

(b) A court order;

(c) A repayment agreement between the holder and a custodial parent; or

(d) A repayment agreement between the holder and a State agency providing child support enforcement services.

§ 120.172 Flood-plain and wetlands management.

(a) All loans must conform to requirements of Executive Orders 11988, ''Flood Plain Management'' (3 CFR, 1977 Comp., p. 117) and 11990, ''Protection of Wetlands'' (3 CFR, 1977 Comp., p. 121). Lenders, Intermediaries, CDCs, and SBA must comply with requirements applicable to them. Applicants must show:

(1) Whether the location for which financial assistance is proposed is in a floodplain or wetland;

(2) If it is in a floodplain, that the assistance is in compliance with local land use plans; and

(3) That any necessary construction or use permits will be issued.

(b) Generally, there is an 8-step decision making process with respect to:

(1) Construction or acquisition of anything, other than a building;

(2) Repair and restoration equal to more than 50% of the market value of a building; or

(3) Replacement of destroyed structures.

(c) SBA may determine for the following types of actions, on a case-by-case basis, that the full 8-step process is not warranted and that only the first step (determining if a proposed action is in the base floodplain) need be completed:

(1) Actions located outside the base floodplain;

(2) Repairs, other than to buildings, that are less than 50% of the market value;

(3) Replacement of building contents, materials, and equipment;

(4) Hazard mitigation measures;

(5) Working capital loans; or

(6) SBA loan assistance of $1,500,000 or less.

§ 120.173 Lead-based paint.

If loan proceeds are for the construction or rehabilitation of a residential structure, lead-based paint may not be used on any interior surface, or on any exterior surface that is readily accessible to children under the age of seven years.

§ 120.174 Earthquake hazards.

When loan proceeds are used to construct a new building or an addition to an existing building, the construction must conform with the ''National Earthquake Hazards Reduction Program (''NEHRP'') Recommended Provisions for the Development of Seismic Regulations for New Buildings'' (which can be obtained from the Federal Emergency Management Agency, Publications Office, Washington, DC) or a code identified by SBA as being substantially equivalent.

§ 120.175 Coastal barrier islands.

SBA and Intermediaries may not make or guarantee any loan within the Coastal Barrier Resource System.

§ 120.176 Compliance with other laws.

All SBA loans are subject to all applicable laws, including (without limitation) the civil rights laws (*see* parts 112, 113, 117 and 136 of this chapter), prohibiting discrimination on the grounds of race, color, national origin, religion, sex, marital status, disability or age. SBA requests agreements or evidence to support or document compliance with these laws, including reports required by applicable statutes or the regulations in this chapter.

Applicability and Enforceability of Loan Program Requirements

§ 120.180 Lender and CDC compliance with Loan Program Requirements.

Lenders must comply and maintain familiarity with Loan Program Requirements for the 7(a) program, as such requirements are revised from time to time. CDCs must comply and maintain familiarity with Loan Program Requirements for the 504 program, as such requirements are revised from time to time. Loan Program Requirements in effect at the time that a

Lender or CDC takes an action in connection with a particular loan govern that specific action. For example, although loan closing requirements in effect when a Lender or CDC closes a loan will govern the closing actions, a Lender or CDC's liquidation actions on the same loan are subject to the liquidation requirements in effect at the time that a liquidation action is taken.

[72 FR 18360, Apr. 12, 2007]

§ 120.181 Status of Lenders and CDCs.

Lenders, CDCs and their contractors are independent contractors that are responsible for their own actions with respect to a 7(a) or 504 loan. SBA has no responsibility or liability for any claim by a borrower, guarantor or other party alleging injury as a result of any allegedly wrongful action taken by a Lender, CDC or an employee, agent, or contractor of a Lender or CDC.

[72 FR 18360, Apr. 12, 2007]

LOAN APPLICATIONS

§ 120.190 Where does an applicant apply for a loan?

An applicant for a business loan should apply to:

(a) A Lender for a guaranteed or immediate participation loan;

(b) A CDC for a 504 loan;

(c) An Intermediary for a Microloan; or

(d) SBA for a direct loan.

§ 120.191 The contents of a business loan application.

For most business loans, SBA requires that an application for a business loan contain, among other things, a description of the history and nature of the business, the amount and purpose of the loan, the collateral offered for the loan, current financial statements, historical financial statements (or tax returns if appropriate) for the past three years, IRS tax verification, and a business plan, when applicable. Personal histories and financial statements will be required from principals of the applicant (and the Operating Company, if applicable).

§ 120.192 Approval or denial.

Applicants receive notice of approval or denial by the Lender, CDC, Intermediary, or SBA, as appropriate. Notice of denial will include the reasons. If a loan is approved, an Authorization will be issued.

§ 120.193 Reconsideration after denial.

An applicant or recipient of a business loan may request reconsideration of a denied loan or loan modification request within 6 months of denial. Applicants denied due to a size determination can appeal that determination under part 121 of this chapter. All others must be submitted to the office that denied the original request. To prevail, the applicant must demonstrate that it has overcome all legitimate reasons for denial. Six months after denial, a new application is required. If the reconsideration is denied, a second and final reconsideration may be considered by the Director, Office of Financial Assistance (D/FA), whose decision is final.

COMPUTERIZED SBA FORMS

§ 120.194 [Reserved]

REPORTING

§ 120.195 Disclosure of fees.

An Applicant for a business loan must identify to SBA the name of each Agent as defined in part 103 of this chapter that helped the applicant obtain the loan, describing the services performed, and disclosing the amount of each fee paid or to be paid by the applicant to the Agent in conjunction with the performance of those services.

§ 120.197 Notifying SBA's Office of Inspector General of suspected fraud.

Lenders, CDCs, Borrowers, and others must notify the SBA Office of Inspector General of any information which indicates that fraud may have occurred in connection with a 7(a) or 504 loan. Send the notification to the Assistant Inspector General for Investigations, Office of Inspector General, U.S. Small Business Administration, 409 3rd Street, SW., Washington, DC 20416.

[72 FR 18360, Apr. 12, 2007]

Subpart B—Policies Specific to 7(a) Loans

BONDING REQUIREMENTS

§ 120.200 What bonding requirements exist during construction?

On 7(a) loans which finance construction, the Borrower must supply a 100 percent payment and performance bond and builder's risk insurance, unless waived by SBA.

LIMITATIONS ON USE OF PROCEEDS

§ 120.201 Refinancing unsecured or undersecured loans.

A Borrower may not use 7(a) loan proceeds to pay any creditor in a position to sustain a loss causing a shift to SBA of all or part of a potential loss from an existing debt.

§ 120.202 Restrictions on loans for changes in ownership.

A Borrower may not use 7(a) loan proceeds to purchase a portion of a business or a portion of another owner's interest. One or more current owners may use loan proceeds to purchase the entire interest of another current owner, or a Borrower can purchase ownership of an entire business.

MATURITIES; INTEREST RATES; LOAN AND GUARANTEE AMOUNTS

§ 120.210 What percentage of a loan may SBA guarantee?

SBA's guarantee percentage must not exceed the applicable percentage established in section 7(a) of the Act. The maximum allowable guarantee percentage on a loan will be determined by the loan amount. Loans of $150,000 or less may receive a maximum guaranty of 85 percent. Loans more than $150,000 may receive a maximum guaranty of 75 percent, except as otherwise authorized by law.

[61 FR 3235, Jan. 31, 1996, as amended at 68 FR 51680, Aug. 28, 2003; 76 FR 63546, Oct. 12, 2011]

§ 120.211 What limits are there on the amounts of direct loans?

(a) The statutory limit for direct loans made under the authority of section 7(a)(1)-(19) of the Small Business Act is $350,000. SBA has established an administrative limit of $150,000 for direct loans. The D/FA may authorize acceptance of an application up to the statutory limit.

(b) The statutory limit for direct loans made under the authority of section 7(a)(20) is $750,000. SBA has established an administrative limit of $150,000. The Associate Administrator for Business Development may authorize the acceptance of an application that exceeds the administrative limit.

(c) The statutory limit on SBA's portion of an immediate participation loan is $350,000. The administrative limit is the lesser of 75 percent of the loan or $150,000. The D/FA may authorize exceptions to the administrative limit up to $350,000.

[61 FR 3235, Jan. 31, 1996, as amended at 74 FR 45753, Sept. 4, 2009]

§ 120.212 What limits are there on loan maturities?

The term of a loan shall be:

(a) The shortest appropriate term, depending upon the Borrower's ability to repay;

(b) Ten years or less, unless it finances or refinances real estate or equipment with a useful life exceeding ten years; and

(c) A maximum of 25 years, including extensions. (A portion of a loan used to acquire or improve real property may have a term of 25 years plus an additional period needed to complete the construction or improvements.)

§ 120.213 What fixed interest rates may a Lender charge?

(a) *Fixed Rates for Guaranteed Loans.* A loan may have a reasonable fixed interest rate. SBA periodically publishes the maximum allowable rate in the FEDERAL REGISTER.

(b) *Direct loans.* A statutory formula based on the cost of money to the Federal government determines the interest rate on direct loans. SBA publishes the rate periodically in the FEDERAL REGISTER.

§ 120.214 What conditions apply for variable interest rates?

A Lender may use a variable rate of interest, upon SBA's approval. SBA's maximum allowable rates apply only

to the initial rate on the date SBA received the loan application. SBA shall approve the use of a variable interest rate under the following conditions:

(a) *Frequency.* The first change may occur on the first calendar day of the month following initial disbursement, using the base rate (see paragraph (c) of this section) in effect on the first business day of the month. After that, changes may occur no more often than monthly.

(b) *Range of fluctuation.* The amount of fluctuation shall be equal to the movement in the base rate. The difference between the initial rate and the ceiling rate may be no greater than the difference between the initial rate and the floor rate.

(c) *Base rate.* The base rate will be one of the following: (i) The prime rate; (ii) the thirty-day (1-month) London Interbank Offered Rate (LIBOR) plus 3 percentage points, or (iii) the Optional Peg Rate. The prime or LIBOR rate will be that which is in effect on the first business day of the month, as printed in a national financial newspaper published each business day. SBA publishes the Optional Peg Rate quarterly in the FEDERAL REGISTER.

(d) *Maturities under 7 years.* For loans with maturities under seven years, the maximum interest rate shall not exceed two and one-quarter (2 1/4) percentage points over the base rate.

(e) *Maturities of 7 years or more.* For loans with maturities of seven or more years, the maximum interest rate shall not exceed two and three-quarters (2 3/4) percentage points over the base rate.

(f) *Amortization.* Initial amortization of principal and interest may be recomputed and reassessed as interest rates fluctuate, as directed by SBA. With prior approval of SBA, the Lender may use certain other amortization methods, except that SBA does not allow balloon payments.

[61 FR 3235, Jan. 31, 1996, as amended at 73 FR 67101, Nov. 13, 2008]

§ 120.215 What interest rates apply to smaller loans?

For a loan over $25,000 but not exceeding $50,000, the interest rate may be one percent more than the maximum interest rate described above. For a loan of $25,000 or less, the maximum interest rate described above may be increased by two percentage points.

[61 FR 3235, Jan. 31, 1996; 61 FR 7986, Mar. 1, 1996]

FEES FOR GUARANTEED LOANS

§ 120.220 Fees that Lender pays SBA.

A Lender must pay a guaranty fee to SBA for each loan it makes. If the guarantee fee is not paid, SBA may terminate the guarantee. Acceptance of the guaranty fee by SBA does not waive any right of SBA arising from a Lender's negligence, misconduct or violation of any provision of these regulations, the guaranty agreement, or the loan authorization.

(a) *Amount of guaranty fee*—(1) *In general.* Except to the extent paragraph (a)(2) of this section applies, for a loan with a maturity of twelve (12) months or less, the guarantee fee which the Lender must pay to SBA is one-quarter (¼) of one percent of the guaranteed portion of the loan. For a loan with a maturity of more than twelve (12) months, the guarantee fee is payable as follows:

(i) Not more than 2 percent of the guaranteed portion of a loan if the total amount of the loan is not more than $150,000;

(ii) Not more than 3 percent of the guaranteed portion of a loan if the total amount of the loan is more than $150,000 but not more than $700,000;

(iii) Except as provided in paragraph (a)(1)(iv) of this section, not more than 3.5 percent of the guaranteed portion of a loan if the total amount of the loan is more than $700,000; and

(iv) An additional 0.25 percent of the guaranteed portion of a loan if the total amount of the loan is more than $1,000,000.

(2) *For loans approved October 1, 2002, through September 30, 2004.* For a loan with a maturity of twelve (12) months or less, the guarantee fee which the Lender must pay to SBA is one-quarter (¼) of one percent of the guaranteed portion of the loan. For a loan with a maturity of more than twelve (12) months, the guarantee fee is:

(i) 1 percent of the guaranteed portion of the loan if the total loan amount is not more than $150,000,

(ii) 2.5 percent of the guaranteed portion of a loan if the total loan amount is more than $150,000, but not more than $700,000, and

(iii) 3.5 percent of the guaranteed portion if the total loan amount is more than $700,000.

(3) *For loans approved under section 7(a)(31) of the Small Business Act (SBA Express loans) to veterans and/or the spouse of a veteran.* In fiscal years when the 7(a) program is at zero subsidy, SBA will not collect a guarantee fee in connection with a loan made under section 7(a)(31) of the Small Business Act to a business owned and controlled by a veteran or the spouse of a veteran.

(b) *When the guaranty fee is payable.* For a loan with a maturity of twelve (12) months or less, the Lender must pay the guaranty fee to SBA electronically within 10 business days after receiving SBA loan approval. The Lender may only charge the Borrower for the fee after the Lender pays the guaranty fee. For a loan with a maturity in excess of twelve (12) months, the Lender must pay the guaranty fee to SBA electronically within 90 days after SBA gives its loan approval. The Lender may charge the Borrower the fee after the Lender has made the first disbursement of the loan. The Borrower may use the loan proceeds to pay the guaranty fee. However, the first disbursement must not be made solely or primarily to pay the guaranty fee.

(c) *Refund of guaranty fee.* For a loan with a maturity of more than twelve (12) months, SBA will refund the guaranty fee if the Lender has not made any disbursement and the lender requests in writing the refund and cancellation of the SBA guaranty.

(d) *Lender's retention of portion of guaranty fee.* With respect to a loan with a maturity of more than twelve (12) months, where the total loan amount is no more than $150,000 Lender may retain not more than 25 percent of the guaranty fee.

(e) If the guarantee fee is not paid, SBA may terminate the guarantee. The Borrower may use working capital loan proceeds to reimburse the Lender for the guarantee fee. Acceptance of the guarantee fee by SBA shall not waive any right of SBA arising from the Lender's misconduct or violation of any provision of this part, the guarantee agreement, the Authorization, or other loan documents.

(f) *Lender's annual service fee payable to SBA*—(1) *In general.* Except to the extent paragraph (f)(2) of this section applies, the lender shall pay SBA an annual service fee in an amount not to exceed 0.55 percent of the outstanding balance of the guaranteed portion of each loan. The service fee cannot be charged to the Borrower. SBA may institute a late fee charge for delinquent payments of the annual service fee to cover administrative costs associated with collecting delinquent fees.

(2) *For loans approved from October 1, 2002, through September 30, 2004.* The lender shall pay SBA an annual service fee equal to 0.25 percent of the outstanding balance of the guaranteed portion of each loan. The service fee cannot be charged to the Borrower. SBA may institute a late fee charge for delinquent payments of the annual service fee to cover administrative costs associated with collecting delinquent fees.

[61 FR 3235, Jan. 31, 1996; 61 FR 11471, Mar. 20, 1996, as amended at 68 FR 51680, Aug. 28, 2003; 68 FR 56554, Oct. 1, 2003; 76 FR 63546, Oct. 12, 2011; 82 FR 39502, Aug. 21, 2017]

§ 120.221 Fees and expenses which the Lender may collect from a loan applicant or Borrower.

Unless otherwise allowed by SBA Loan Program Requirements, the Lender may charge and collect from the applicant or Borrower only the following fees and expenses:

(a) *Service and packaging fees.* The Lender may charge an applicant reasonable fees (customary for similar Lenders in the geographic area where the loan is being made) for packaging and other services. The Lender must advise the applicant in writing that the applicant is not required to obtain or pay for unwanted services. The applicant is responsible for deciding whether fees are reasonable. SBA may review these fees at any time. Lender must refund any such fee considered unreasonable by SBA.

(b) *Extraordinary servicing.* Subject to prior written SBA approval, if all or part of a loan will have extraordinary servicing needs, the Lender may charge

the applicant a service fee not to exceed 2 percent per year on the outstanding balance of the part requiring special servicing.

(c) *Out-of-pocket expenses.* The Lender may collect from the applicant necessary out-of-pocket expenses such as filing or recording fees.

(d) *Late payment fee.* The Lender may charge the Borrower a late payment fee not to exceed 5 percent of the regular loan payment.

(e) *Legal services.* Lender may charge the Borrower for legal services rendered on an hourly basis.

[61 FR 3235, Jan. 31, 1996, as amended at 82 FR 39503, Aug. 21, 2017]

§ 120.222 Prohibition on sharing premiums for secondary market sales.

The Lender or its Associates may not share in any premium received from the sale of an SBA guaranteed loan in the secondary market with a Service Provider, packager, or other loan-referral source.

[82 FR 39503, Aug. 21, 2017]

§ 120.223 Subsidy recoupment fee payable to SBA by Borrower.

(a) The subsidy recoupment fee is payable to SBA when:

(1) Loan has a maturity of 15 years or more.

(2) Borrower makes a voluntary prepayment (or several prepayments in the aggregate) during any one of the first three successive 12 month periods following the first disbursement of the loan. Prepayment is defined as a payment of principal in excess of the amount due according to the amortization schedule.

(3) The prepayment (or several prepayments in the aggregate) is more than 25 percent of the highest outstanding principal balance of the loan in any one of the first three successive 12 month periods following the first disbursement.

(b) When all the conditions above exist, the following subsidy recoupment fees apply:

(1) If the prepayment is made during the first 12 month period after first disbursement, the charge is 5 percent of the total amount of all prepayments made during such period;

(2) If the prepayment is made during the second 12 month period after first disbursement, the charge is 3 percent of the total amount of all prepayments made during that period; and

(3) If the prepayment is made during the third 12 month period after first disbursement, the charge is 1 percent of the total amount of all prepayments made during that period.

[68 FR 51680, Aug. 28, 2003]

Subpart C—Special Purpose Loans

§ 120.300 Statutory authority.

Congress has authorized several special purpose programs in various subsections of section 7(a) of the Act. Generally, 7(a) loan policies, eligibility requirements and credit criteria enumerated in subpart B of this part apply to these programs. The sections of this subpart prescribe the special conditions applying to each special purpose program. As with other business loans, special purpose loans are available only to the extent funded by annual appropriations.

DISABLED ASSISTANCE LOAN PROGRAM (DAL)

§ 120.310 What assistance is available for the disabled?

Section 7(a)(10) of the Act authorizes SBA to guarantee or make direct loans to the disabled. SBA distinguishes two kinds of assistance:

(a) *DAL–1.* DAL–1 Financial Assistance is available to non-profit public or private organizations for disabled individuals that employ such individuals; or

(b) *DAL–2.* DAL–2 Financial Assistance is available to:

(1) Small businesses wholly owned by disabled individuals; and

(2) Disabled individuals to establish, acquire, or operate a small business.

§ 120.311 Definitions.

(a) *Organization for the disabled* means one which:

(1) Is organized under federal or state law to operate in the interest of disabled individuals;

(2) Is non-profit;

(3) Employs disabled individuals for seventy-five percent of the time needed

to produce commodities or services for sale; and

(4) Complies with occupational and safety standards prescribed by the Department of Labor.

(b) *Disabled individual* means a person who has a permanent physical, mental or emotional impairment, defect, ailment, disease or disability which limits the type of employment for which the person would otherwise be qualified.

§ 120.312 DAL–1 use of proceeds and other program conditions.

(a) DAL–1 applicants must submit appropriate documents to establish program eligibility.

(b) Generally, applicants may use loan proceeds for any 7(a) loan purposes. Loan proceeds may not be used:

(1) To purchase or construct facilities if construction grants and mortgage assistance are available from another Federal source; or

(2) For supportive services (expenses incurred by a DAL–1 organization to subsidize wages of low producers, health and rehabilitation services, management, training, education, and housing of disabled workers).

(c) SBA does not consider a DAL–1 organization to have a conflict of interest if one or more of its Associates is an Associate of the Lender.

§ 120.313 DAL–2 use of proceeds and other program conditions.

(a) The DAL–2 loan proceeds may be used for any 7(a) loan purposes.

(b) An applicant may use DAL–2 loan proceeds to acquire an eligible small business without complying with the change of ownership conditions in § 120.202.

(c) A DAL–2 applicant must submit evidence from a physician, psychiatrist, or other qualified professional as to the permanent nature of the disability and the limitation it places on the applicant.

§ 120.314 Resolving doubts about creditworthiness.

For the purpose of the DAL Program, SBA shall resolve doubts concerning the creditworthiness of an applicant in favor of the applicant. However, the applicant must present satisfactory evidence of repayment ability. Personal guarantees of Associates are not required for purposes of DAL–1 financial assistance.

§ 120.315 Interest rate and loan limit.

The interest rate on direct DAL loans is three percent. There is an administrative limit of $150,000 on a direct DAL loan.

Businesses Owned by Low Income Individuals

§ 120.320 Policy.

Section 7(a)(11) of the Act authorizes SBA to guarantee or make direct loans to establish, preserve or strengthen small business concerns:

(a) Located in an area having high unemployment according to the Department of Labor;

(b) Located in an area in which a high percentage of individuals have a low income inadequate to satisfy basic family needs; and

(c) More than 50 percent owned by low income individuals.

Energy Conservation

§ 120.330 Who is eligible for an energy conservation loan?

SBA may make or guarantee loans to assist a small business to design, engineer, manufacture, distribute, market, install, or service energy devices or techniques designed to conserve the Nation's energy resources.

§ 120.331 What devices or techniques are eligible for a loan?

Eligible energy conservation devices or techniques include:

(a) Solar thermal equipment;

(b) Photovoltaic cells and related equipment;

(c) A product or service which increases the energy efficiency of existing equipment, methods of operation or systems which use fossil fuels, and which is on the Energy Conservation Measures list of the Secretary of Energy;

(d) Equipment producing energy from wood, biological waste, grain or other biomass energy sources;

(e) Equipment for cogeneration of energy, district heating or production of energy from industrial waste;

(f) Hydroelectric power equipment;

(g) Wind energy conversion equipment; and

(h) Engineering, architectural, consulting, or other professional services necessary or appropriate for any of the devices or techniques in paragraphs (a) through (g) of this section.

§ 120.332 What are the eligible uses of proceeds?

(a) *Acquire property.* The Borrower may use the loan proceeds to acquire land necessary for imminent plant construction, buildings, machinery, equipment, furniture, fixtures, facilities, supplies, and material needed to accomplish any of the eligible program purposes in § 120.330.

(b) *Research and development.* Up to 30% of loan proceeds may be used for research and development:

(1) Of an existing product or service; or

(2) A new product or service.

(c) *Working capital.* The Borrower may use proceeds for working capital for entering or expanding in the energy conservation market.

§ 120.333 Are there any special credit criteria?

In addition to regular credit evaluation criteria, SBA shall weigh the greater risk associated with energy projects. SBA shall consider such factors as quality of the product or service, technical qualifications of the applicant's management, sales projections, and financial status.

EXPORT WORKING CAPITAL PROGRAM (EWCP)

§ 120.340 What is the Export Working Capital Program?

Under the EWCP, SBA guarantees short-term working capital loans made by participating lenders to exporters (section 7(a)(14) of the Act). Loan maturities may be for up to three years with annual renewals. Proceeds can be used only to finance export transactions. Loans can be for single or multiple export transactions. An export transaction is the production and payment associated with a sale of goods or services to a foreign buyer. The maximum loan amount for any one EWCP loan is $5,000,000. EWCP loans shall receive a guaranty of 90 percent, not to exceed $4,500,000.

[61 FR 3235, Jan. 31, 1996, as amended at 76 FR 63546, Oct. 12, 2011]

§ 120.341 Who is eligible?

In addition to the eligibility criteria applicable to all 7(a) loans, an applicant must be in business for one full year at the time of application, but not necessarily in the exporting business. SBA may waive this requirement if the applicant has sufficient export trade experience or other managerial experience.

§ 120.342 What are eligible uses of proceeds?

Loan proceeds may be used:

(a) To acquire inventory;

(b) To pay the manufacturing costs of goods for export;

(c) To purchase goods or services for export;

(d) To support standby letters of credit;

(e) For pre-shipment working capital; and

(f) For post-shipment foreign accounts receivable financing.

§ 120.343 Collateral.

A Borrower must give SBA a first security interest sufficient to cover 100 percent of the EWCP loan amount (such as insured accounts receivable or letters of credit). Collateral must be located in the United States, its territories or possessions.

§ 120.344 Unique requirements of the EWCP.

(a) An applicant must submit cash flow projections to support the need for the loan and the ability to repay. After the loan is made, the loan recipient must submit continual progress reports.

(b) SBA does not limit the amount of extraordinary servicing fees, as referenced in § 120.221(b), under the EWCP.

(c) SBA does not prescribe the interest rates for the EWCP, but will monitor these rates for reasonableness.

INTERNATIONAL TRADE LOANS

§ 120.345 Policy.

Section 7(a)(16) of the Act authorizes SBA to guarantee loans to small businesses that are:

(a) Engaged or preparing to engage in international trade; or

(b) Adversely affected by import competition.

§ 120.346 Eligibility.

(a) An applicant must establish that:

(1) The loan proceeds will significantly expand an existing export market or develop new export markets; or

(2) The applicant business is adversely affected by import competition; and

(3) The loan will improve the applicant's competitive position.

(b) The applicant must have a business plan reasonably supporting its projected export sales.

[61 FR 3235, Jan. 31, 1996, as amended at 76 FR 63546, Oct. 12, 2011]

§ 120.347 Use of proceeds.

The Borrower may use loan proceeds to acquire, construct, renovate, modernize, improve, or expand facilities and equipment to be used in the United States to produce goods or services involved in international trade, and to develop and penetrate foreign markets. The Borrower may also use proceeds in the refinancing of existing indebtedness that is not structured with reasonable terms and conditions, including any debt that qualifies for refinancing under 7(a) Loan Program Requirements, and to provide working capital.

[61 FR 3235, Jan. 31, 1996, as amended at 76 FR 63546, Oct. 12, 2011]

§ 120.348 Amount of guarantee.

The maximum loan amount for any one International Trade (IT) loan is $5,000,000. IT loans may receive a maximum guaranty of 90 percent or $4,500,000, except that the maximum guaranty amount for any working capital component of an IT loan is limited to $4,000,000. To the extent that the Borrower has a separate EWCP loan or any other 7(a) loan for working capital, the guaranty amount for the other loan is counted against the $4,000,000 guaranty limit for the IT loan.

[76 FR 63546, Oct. 12, 2011]

§ 120.349 Collateral.

Each IT loan must be secured either by a first lien position or first mortgage on the property or equipment financed by the IT loan or on other assets of the Borrower, except that an IT loan may be secured by a second lien position on the property or equipment financed by the IT loan or on other assets of the Borrower, if the SBA determines the second lien position provides adequate assurance of the payment of the IT loan.

[76 FR 63546, Oct. 12, 2011]

QUALIFIED EMPLOYEE TRUSTS (ESOP)

§ 120.350 Policy.

Section 7(a)(15) of the Act authorizes SBA to guarantee a loan to a qualified employee trust (''ESOP'') to:

(a) Help finance the growth of its employer's small business; or

(b) Purchase ownership or voting control of the employer.

§ 120.351 Definitions.

All terms specific to ESOPs have the same definition for purposes of this section as in the Internal Revenue Service (IRS) Code (title 26 of the United States Code) or regulations (26 CFR chapter I).

§ 120.352 Use of proceeds.

Loan proceeds may be used for two purposes.

(a) *Qualified employer securities.* A qualified employee trust may relend loan proceeds to the employer by purchasing qualified employer securities. The small business concern may use these funds for any general 7(a) purpose.

(b) *Control of employer.* A qualified employee trust may use loan proceeds to purchase a controlling interest (51 percent) in the employer. Ownership and control must vest in the trust by the time the loan is repaid.

§ 120.353 Eligibility.

SBA may assist a qualified employee trust (or equivalent trust) that meets

the requirements and conditions for an ESOP prescribed in all applicable IRS, Treasury and Department of Labor (DOL) regulations. In addition, the following conditions apply:

(a) The small business must provide the funds needed by the trust to repay the loan; and

(b) The small business must provide adequate collateral.

§ 120.354 Creditworthiness.

In determining repayment ability, SBA shall not consider the personal assets of the employee-owners of the trust. SBA shall consider the earnings history and projected future earnings of the employer small business. SBA may consider the business and management experience of the employee-owners.

VETERANS LOAN PROGRAM

§ 120.360 Which veterans are eligible?

SBA may guarantee or make direct loans to a small business 51 percent owned by one or more of the following eligible veterans:

(a) Vietnam-era veterans who served for a period of more than 180 days between August 5, 1964, and May 7, 1975, and were discharged other than dishonorably;

(b) Disabled veterans of any era with a minimum compensable disability of 30 percent; or

(c) A veteran of any era who was discharged for disability.

§ 120.361 Other conditions of eligibility.

(a) Management and daily operations of the business must be directed by one or more of the veteran owners whose veteran status was used to qualify for the loan.

(b) This direct loan program is available only if private sector financing and guaranteed loans are not available.

(c) A veteran may qualify only once for this program on a direct loan basis.

POLLUTION CONTROL PROGRAM

§ 120.370 Policy.

Section 7(a)(12) of the Act authorizes SBA to guarantee loans up to $1,000,000 to an eligible small business to plan, design or install a pollution control facility. An applicant must meet the eligibility requirements for 7(a) loans.

LOANS TO PARTICIPANTS IN THE 8(a) PROGRAM

§ 120.375 Policy.

Section 7(a)(20) of the Act authorizes SBA to provide direct (unilaterally or together with Lenders) or guaranteed loans to firms participating in the 8(a) Program.

§ 120.376 Special requirements.

The following special conditions apply (otherwise, 7(a) loan eligibility criteria apply):

(a) The Associate Administrator for Business Development may waive the direct loan administrative ceiling of $150,000, and raise it to $750,000.

(b) The SBA portion of a guaranteed loan must not exceed $750,000.

(c) The interest rate on a guaranteed loan shall be the same as on 7(a) guaranteed business loans. The interest rate on a direct loan shall be one percent less than on a regular direct loan.

(d) For a direct loan or SBA's portion of an immediate participation loan, SBA shall subordinate its security interest on all collateral to other debt of the applicant.

[61 FR 3235, Jan. 31, 1996, as amended at 74 FR 45753, Sept. 4, 2009]

§ 120.377 Use of proceeds.

The loan proceeds shall not be used for debt refinancing. Only a manufacturing concern may use loan proceeds for working capital.

DEFENSE ECONOMIC TRANSITION ASSISTANCE

§ 120.380 Program.

Section 7(a)(21) of the Act authorizes SBA to guarantee loans to help eligible small businesses transition from defense to civilian markets, or eligible individuals adversely impacted by base closures or defense cutbacks to acquire or open and operate a small business.

§ 120.381 Eligibility.

(a) *Eligible small businesses.* A small business is eligible if it has been detrimentally impacted by the closure (or

substantial reduction) of a Department of Defense installation, or the termination (or substantial reduction) of a Department of Defense Program on which the small business was a prime contractor, subcontractor, or supplier at any tier.

(b) *Eligible individual.* An eligible individual, for purposes of this program, includes the following persons involuntarily separated from their position or voluntarily terminated under a program offering inducements to encourage early retirement:

(1) A member of the Armed Forces of the United States (honorably discharged);

(2) A civilian employee of the Department of Defense; or

(3) An employee of a prime contractor, sub-contractor, or supplier at any tier of a Department of Defense program.

(c) *Defense loan and technical assistance (DELTA).* The DELTA program provides financial and technical assistance to defense dependent small businesses which have been adversely affected by defense reductions. The goal of the program is to assist these businesses to diversify into the commercial market while remaining part of the defense industrial base. Complete information on eligibility and other rules is available from each SBA district office.

§ 120.382 Repayment ability.

SBA shall resolve reasonable doubts concerning the small business' proposed business plan for transition to non-defense-related markets in favor of the loan applicant in determining the sound value of the proposed loan.

§ 120.383 Restrictions on loan processing.

Since greater risk may be associated with a loan to an applicant under this program, a Certified Lender or Preferred Lender shall not make a defense economic assistance loan under the PLP or CLP programs.

CAPLINES PROGRAM

§ 120.390 Revolving credit.

(a) CapLines finances eligible small businesses' short-term, revolving and non-revolving working-capital needs. SBA regulations governing the 7(a) loan program govern business loans made under this program. The maximum guaranteed amount and the maximum loan amount are the same under CapLines as other 7(a) loans, as stated in § 120.151.

(b) CapLines proceeds can be used to finance the cyclical, recurring, or other identifiable short-term operating capital needs of small businesses. Proceeds can be used to create current assets or used to provide financing against the current assets that already exist.

[61 FR 3235, Jan. 31, 1996, as amended at 76 FR 63546, Oct. 12, 2011]

BUILDERS LOAN PROGRAM

§ 120.391 What is the Builders Loan Program?

Under section 7(a)(9) of the Act, SBA may make or guarantee loans to finance small general contractors to construct or rehabilitate residential or commercial property for resale. This program provides an exception under specified conditions to the general rule against financing investment property. ''Construct'' and ''rehabilitate'' mean only work done on-site to the structure, utility connections and landscaping.

§ 120.392 Who may apply?

A construction contractor or homebuilder with a past history of profitable construction or rehabilitation projects of comparable type and size may apply. An applicant may subcontract the work. Subcontracts in excess of $25,000 may require 100 percent payment and performance bonds.

§ 120.393 Are there special application requirements?

(a) An applicant must submit documentation from:

(1) A mortgage lender indicating that permanent mortgage money is available to qualified purchasers to buy such properties;

(2) A real estate broker indicating that a market exists for the proposed building and that it will be compatible with its neighborhood; and

(3) An architect, appraiser or engineer agreeing to make inspections and

certifications to support interim disbursements.

(b) The Borrower may substitute a letter from a qualified Lender for one or more of the letters.

§ 120.394 What are the eligible uses of proceeds?

A Borrower must use the loan proceeds solely to acquire, construct or substantially rehabilitate an individual residential or commercial building for sale. ''Substantial'' means rehabilitation expenses of more than one-third of the purchase price or fair market value at the time of the application. A Borrower may use up to 33 percent of the proceeds to acquire land, and up to 5 percent for community improvements such as curbs and sidewalks.

[61 FR 3235, Jan. 31, 1996, as amended at 82 FR 39503, Aug. 21, 2017]

§ 120.395 What is SBA's collateral position?

SBA will require a lien on the building which must be in no less than a second position.

§ 120.396 What is the term of the loan?

The loan must not exceed sixty (60) months plus the estimated time to complete construction or rehabilitation.

§ 120.397 Are there any special restrictions?

The borrower must not use loan proceeds to purchase vacant land for possible future construction or to operate or hold rental property for future rehabilitation. SBA may allow rental of the property only if the rental will improve the ability to sell the property. The sale must be a legitimate change of ownership.

AMERICA'S RECOVERY CAPITAL (BUSINESS STABILIZATION) LOAN PROGRAM—ARC LOAN PROGRAM

§ 120.398 America's Recovery Capital (ARC) Loan Program.

(a) *Purpose.* The purpose of the ARC Loan Program is to enable SBA to guarantee certain loans to viable small businesses that are experiencing immediate financial hardship. Loans made under this loan program are referred to as ARC Loans and are subject to the requirements set forth in this Part for 7(a) loans except as noted in this section.

(b) *Definitions.* (1) (i) *Eligible Borrower* is a small business concern as defined in Section 3 of the Small Business Act and § 120.100. Eligible Borrower does not include:

(A) Ineligible small businesses as listed in § 120.110; and

(B) Small business concerns with the following primary industry North American Industry Classification System (NAICS) codes:

(*1*) 713210 (Casinos (Except Casino Hotels));

(*2*) 721120 (Casino Hotels);

(*3*) 713290 (Other Gambling Industries);

(*4*) 713910 (Golf Courses and Country Clubs); and

(*5*) 712130 (Zoos and Botanical Gardens).

(ii) Applications submitted by small business concerns with a primary industry NAICS code of 713940 (Fitness and Recreational Sports Centers) will be identified and reviewed by SBA to determine eligibility in accordance with the statutory restriction on assistance to swimming pools.

(2) *Going Concern* is a small business concern actively engaging in business with the expectation of indefinite continuance.

(3) *Qualifying Small Business Loan* is a loan previously made to an Eligible Borrower for any of the purposes set forth in § 120.120 and not for any of the purposes set forth in § 120.130 or 120.160(d). Qualifying Small Business Loans may include credit card obligations, capital leases for major equipment and vehicles, notes payable to vendors or suppliers, loans in the first lien position made by commercial lenders in connection with the Development Company Loan Program (504), home equity loans used to finance business operations, other loans to small businesses made without an SBA guaranty, and loans made by or with an SBA guaranty on or after February 17, 2009. Loans made or guaranteed by SBA before February 17, 2009 are not Qualifying Small Business Loans for the purposes of the ARC Loan Program. A

Qualifying Small Business Loan may not be used as the basis for more than one ARC Loan but ARC Loans may be used to pay multiple Qualifying Small Business Loans.

(4) *Viable small business* is a small business that is a Going Concern but which is having difficulty making periodic payments of principal and interest on Qualifying Small Business Loan(s) and/or meeting operating expenses of the business although it can reasonably demonstrate its projected continued operation for a reasonable period beyond the six month period of payment assistance with an ARC Loan.

(c) *Period of program.* The ARC Loan Program is authorized through September 30, 2010, or until appropriated funds are exhausted, whichever is sooner.

(d) *Use of proceeds.* Loans made under the ARC Loan Program are for the sole purpose of making periodic payments of principal and interest (including default interest), in full or in part, for up to six (6) months, on one or more existing Qualifying Small Business Loans. ARC Loan proceeds cannot be used to make payments on loans made or guaranteed by SBA prior to February 17, 2009.

(e) *Loan terms.* (1) *Guaranty percentage.* ARC Loans are 100% guaranteed by SBA.

(2) *Maximum loan size.* An ARC Loan may not exceed $35,000.

(3) *Interest rate.* The interest rate for ARC Loans will be published by SBA in the FEDERAL REGISTER.

(4) *Loan maturity.* An ARC Loan may be made with a maturity of up to six and one-half years.

(5) *Disbursement period.* The disbursement period for an ARC Loan is up to six consecutive months.

(6) *Loan payments.*

(i) *Borrower's payments.* The borrower will be responsible for all principal payments.

(ii) *Payment of interest by SBA.* SBA will make periodic interest payments to the lender on ARC Loans. Interest will accrue only until the date 120 days after the earliest uncured payment default on the ARC Loan. However, the amount paid by SBA on a defaulted ARC Loan, when it honors its guarantee, will be adjusted to reconcile for any overpayments or underpayments of interest previously paid to the Lender. Interim adjustments to interest paid by SBA to lenders may be made during the term of the ARC Loan and interest payments due the Lender will be adjusted to accommodate the interim interest adjustments.

(iii) *Deferral period.* No principal repayment is required during the disbursement period or for 12 months following the final loan disbursement.

(iv) *Repayment period.* The borrower will be required to pay the loan principal over five years beginning in the 13th month following the final loan disbursement. The ARC Loan balance will be fully amortized over the five year repayment period. Balloon payments may not be required by lenders. The borrower may prepay all or a portion of the principal during the life of the loan without penalty.

(f) *Number of ARC Loans per small business.* No small business may obtain more than one ARC Loan, but the proceeds of the ARC loan may be used to pay more than one Qualifying Small Business Loan.

(g) *Personal guarantees.* Holders of at least a 20 percent ownership interest in the borrower generally must guarantee the ARC Loan.

(h) *Collateral.* SBA requires each lender to follow the collateral policies and procedures that it has established and implemented for similarly-sized non-SBA guaranteed commercial loans. The lender's collateral policies must be commercially reasonable and prudent. Lenders will certify that the collateral policies applied to the ARC Loan meet this standard. Lenders may charge borrowers the direct cost of securing and liquidating collateral for ARC Loans. SBA will reimburse Lenders for the direct cost of liquidating collateral that are not reimbursed by the borrower in the event of default. Reimbursement of the direct costs of liquidation by SBA to the Lender is limited to the amount of the recovery received on the ARC Loan.

(i) *Credit criteria.* To be approved for an ARC Loan, the applicant must be a creditworthy small business with a reasonable expectation of repayment, taking into consideration the following:

(1) Character, reputation, and credit history of the applicant (and the Operating Company, if applicable) and its Associates;

(2) Experience and depth of management;

(3) Strength of the business;

(4) Past earnings, current earnings, and projected cash flow; and

(5) Ability to repay the loan with earnings from the business.

(j) *Statement of hardship.* In addition to the certifications required for 7(a) loans generally, ARC Loan recipients must submit a statement certifying that they are experiencing immediate financial hardship and provide documentation to support the certification.

(k) *Loan application.* The provisions of §120.191 do not apply for ARC Loans. A lender making an ARC Loan will provide an application with information on the small business that includes the nature and history of the business, current and historical financial statements (or tax returns), and other information that SBA may require.

(l) *Preferences and refinancing.* A lender may make an ARC Loan to an Eligible Borrower that intends to use the proceeds of the ARC Loan to make periodic payments of principal and interest on a Qualifying Small Business Loan that is owned or serviced by that same lender. The provisions of §§120.10, 120.536(a)(2) and 120.925 with regard to Preference for repayments without prior SBA approval do not apply to ARC Loans. The provisions of §120.201 restricting refinancing also do not apply to ARC Loans.

(m) *Loan fees.* Neither the lender nor SBA shall impose any fees or direct costs on a borrower of an ARC Loan, except that lenders may charge borrowers for the direct costs of securing and liquidating collateral for the ARC Loan. Fees include, but are not limited to, points, bonus points, prepayment penalties, brokerage fees, fees for processing, origination, or application, and out of pocket expenses (other than the direct costs of securing and liquidating collateral). SBA will not impose any fees on a lender making an ARC Loan.

(n) *Lender reporting.* Lenders shall report on its ARC Loans in accordance with requirements established by SBA from time to time for 7a loans and loans made under the American Recovery and Reinvestment Act of 2009.

(o) *Loan servicing.* Each originating lender shall service all of its ARC Loans in accordance with the existing practices and procedures that the Lender uses for its non-SBA guaranteed commercial loans. In all circumstances, such practices and procedures must be commercially reasonable and consistent with prudent lending standards and in accordance with SBA Loan Program Requirements as defined in §120.10. SBA's prior written consent is required for servicing actions that may have significant exposure implications for SBA. SBA may require written notice of other servicing actions it considers necessary for portfolio management purposes.

(p) *Liquidations.* Each Lender shall be responsible for liquidating any defaulted ARC Loan originated by the Lender. ARC Loans will be liquidated in accordance with the existing practices and procedures that the Lender uses for its non-SBA guaranteed commercial loans. In all circumstances, such practices and procedures must be commercially reasonable and consistent with prudent lending standards and in accordance with SBA Loan Program Requirements as defined in Section 120.10. Loans with de minimis value may, at the Lender's request and with SBA's approval, be liquidated by SBA or its agent(s). Significant liquidation actions taken on ARC Loans must be documented. The reimbursement of liquidation related fees by SBA to the Lender is limited to the amount of the recovery on the ARC Loan.

(q) *Purchase requests.* Any purchase request to SBA to honor its guaranty on a defaulted ARC Loan shall be made by the originating lender. Lenders may request SBA to purchase an ARC Loan when there has been an uncured payment default exceeding 60 days or when the borrower has declared bankruptcy. SBA requires Lenders to submit loans for purchase no later than 120 days after the earliest uncured payment default on the ARC Loan. Additionally, SBA may honor its guarantee and require a Lender to submit an ARC Loan for purchase at any time. Except as noted above, the Lender is required to

complete all recovery actions on the ARC Loan after purchase.

(r) *Prohibition on secondary market sales and loan participations.* A lender may not sell an ARC loan into the secondary market nor may a lender participate a portion of an ARC loan with another lender.

(s) *Loan volume.* SBA reserves the right to allocate loan volume under the ARC Loan Program among Lenders (as defined in § 120.10).

(t) *Delegated authority.* SBA may allow lenders to use their delegated authority to process ARC Loans.

(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* § 120.440(c) concerning Supplemental Guarantee Agreements.

[61 FR 3235, Jan. 31, 1996, as amended at 82 FR 39503, Aug. 21, 2017]

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, 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 its state regulator and be considered Satisfactory by its Federal Financial Institution Regulator (as determined by SBA and based on, for example, information in published orders/agreements and call reports); 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; 82 FR 39503, Aug. 21, 2017]

§ 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.

§ 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, 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.

(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 uncollectible 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 ''nondepository 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, 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.

§ 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, 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 multiparty 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, Feb. 10, 1999, as amended at 73 FR 75511, Dec. 11, 2008; 82 FR 39503, Aug. 21, 2017]

§ 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 probation 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 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, 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.

§ 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, 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, 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, Feb. 10, 1999, as amended at 73 FR 75511, Dec. 11, 2008; 82 FR 39503, Aug. 21, 2017]

§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 considered in determining satisfactory SBA performance. Other factors may include, but are not limited to, 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, Feb. 10, 1999, as amended at 73 FR 75511, Dec. 11, 2008; 82 FR 39503, Aug. 21, 2017]

§ 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, Feb. 10, 1999, as amended at 73 FR 75511, Dec. 11, 2008]

DELEGATED AUTHORITY CRITERIA

§ 120.440 How does a 7(a) Lender obtain delegated authority?

(a) In making its decision to grant or renew a delegated authority, SBA considers whether the Lender, as determined by SBA in its discretion:

(1) Has the continuing ability to evaluate, process, close, disburse, service, liquidate and litigate SBA loans. This includes the ability to develop and analyze complete loan packages. SBA may consider the experience and capability of Lender's management and staff.

(2) Has satisfactory SBA performance (as defined in § 120.410(a)(2));

(3) Is in compliance with SBA Loan Program Requirements (*e.g.*, Form 1502 reporting, timely payment of all fees to SBA);

(4) Has completed to SBA's satisfaction all required corrective actions;

(5) Whether Lender is subject to any enforcement action, order or agreement with a regulator or the presence of other regulatory concerns as determined by SBA; and

(6) Whether Lender exhibits other risk factors (*e.g.*, has rapid growth; low SBA activity; SBA loan volume; Lender, an officer or director is under investigation or indictment).

(b) Delegated authority decisions are made by the appropriate SBA official in accordance with Delegations of Authority, and are final.

(c) If delegated authority is approved or renewed, Lender must execute a Supplemental Guarantee Agreement, which will specify a term not to exceed two years. SBA may grant shortened renewals based on risk or any of the other delegated authority criteria. Lenders with less than 3 years of SBA lending experience will be limited to a term of 1 year or less.

[82 FR 39503, Aug. 21, 2017]

§ 120.441 [Reserved]

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 [Reserved]

§ 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 fo 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;

(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 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 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.

(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, bylaws, 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 principals, 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 $6,623 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, as amended at 81 FR 31491, May 19, 2016; 82 FR 9969, Feb. 9, 2017; 83 FR 7363, Feb. 21, 2018; 84 FR 12061, Apr. 1, 2019]

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 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;

(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 personal 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. The report should accompany requested documentation that SBA deems sufficient to be able to review the Lender's administration of the loan under § 120.524. A Lender's failure to provide sufficient documentation may constitute a material failure to comply with SBA requirements under § 120.524(a)(1), and may lead to initiation of an action for recovery from the Lender of all or some of the moneys SBA paid to a Registered Holder on a guarantee. SBA will also evaluate the Lender's continued participation in the Secondary Market and may restrict further sale of guaranteed portions into the Secondary Market until SBA determines that the Lender has provided sufficient documentation for purchases.

(d) *No waiver of SBA's rights.* Purchase by SBA of the guaranteed portion of a loan, or of a portion of SBA's guarantee of a loan, either through a negotiated agreement with a Lender or otherwise, does not waive any of SBA's rights to recover from the responsible Lender any money paid on the guarantee based upon the occurrence of any of the events set forth in § 120.524(a) in connection with that loan.

[72 FR 18360, Apr. 12, 2007]

§ 120.521 What interest rate applies after SBA purchases its guaranteed portion?

When SBA purchases the guaranteed portion of a fixed interest rate loan, the rate of interest remains as stated in the note. On loans with a fluctuating interest rate, the interest rate that the Borrower owes will be at the rate in effect at the time of the earliest

uncured payment default, or the rate in effect at the time of purchase (where no default has occurred).

§ 120.522 Payment of accrued interest to the Lender or Registered Holder when SBA purchases the guaranteed portion.

(a) *Rate of interest*. If SBA purchases the guaranteed portion from a Lender or from a Registered Holder (if sold in the Secondary Market), it will pay accrued interest at:

(1) The rate in the note if it is a fixed rate loan; or

(2) The rate in effect on the date of the earliest uncured payment default, or of SBA's purchase (if there has been no default).

(b) *Payment to Lender*—(1) *For loans approved on or after May 14, 2007*. SBA will pay up to a maximum of 120 days interest to a Lender at the time of guarantee purchase.

(2) *For loans approved before May 14, 2007*. The regulations applicable to the amount of interest that SBA will pay to a Lender upon loan default that were in effect immediately prior to this date will govern such loans.

(c) *Payment to Registered Holder*. SBA will pay a Registered Holder all accrued interest up to the date of payment.

[61 FR 3235, Jan. 31, 1996, as amended at 72 FR 18361, Apr. 12, 2007]

§ 120.523 What is the "earliest uncured payment default"?

The earliest uncured payment default is the date of the earliest failure by a Borrower to pay a regular installment of principal and/or interest when due. Payments made by the Borrower before a Lender makes its request to SBA to purchase are applied to the earliest uncured payment default. If the installment is paid in full, the earliest uncured payment default date will advance to the next unpaid installment date. If a Borrower makes any payment after the Lender makes its request to SBA to purchase, the earliest uncured payment default date does not change because the Lender has already exercised its right to request purchase.

§ 120.524 When is SBA released from liability on its guarantee?

(a) SBA is released from liability on a loan guarantee (in whole or in part, within SBA's exclusive discretion), if any of the events below occur:

(1) The Lender has failed to comply materially with any Loan Program Requirement for 7(a) loans.

(2) The Lender has failed to make, close, service, or liquidate a loan in a prudent manner;

(3) The Lender's improper action or inaction has placed SBA at risk;

(4) The Lender has failed to disclose a material fact to SBA regarding a guaranteed loan in a timely manner;

(5) The Lender has misrepresented a material fact to SBA regarding a guaranteed loan;

(6) SBA has received a written request from the Lender to terminate the guarantee;

(7) The Lender has not paid the guarantee fee within the period required under SBA rules and regulations;

(8) The Lender has failed to request that SBA purchase a guarantee within 180 days after maturity of the loan. However, if the Lender is conducting liquidation or debt collection litigation in connection with a loan that has matured, SBA will be released from its guarantee only if the Lender fails to request that SBA purchase the guarantee within 180 days after the completion of the liquidation or debt collection litigation;

(9) The Lender has failed to use required SBA forms or exact electronic copies; or

(10) The Borrower has paid the loan in full.

(b) If SBA determines, at any time, that any of the events set forth in paragraph (a) of this section occurred in connection with that loan, SBA is entitled to recover any moneys paid on the guarantee plus interest from the Lender. In the exercise of its rights, SBA may utilize all legal means available, including offset and judicial remedies.

(c) If the Lender's loan documentation or other information indicates that one or more of the events in paragraph (a) of this section occurred, SBA may undertake such investigation as it deems necessary to determine whether

to honor or deny the guarantee, and may withhold a decision on whether to honor the guarantee until the completion of such investigation.

(d) Any information provided to SBA by a Lender or other party will not prejudice, or be construed as effecting any waiver of, SBA's right to deny liability for a guarantee if one or more of the events listed in paragraph (a) of this section occur.

(e) Unless SBA provides written notice to the contrary, the Lender remains responsible for all loan servicing ad liquidation actions until SBA honors its guarantee in full.

[61 FR 3235, Jan. 31, 1996, as amended at 72 FR 18361, Apr. 12, 2007; 82 FR 39503, Aug. 21, 2017]

§ 120.530 Deferment of payment.

SBA may agree to defer payments on a business loan for a stated period of time, and use such other methods as it considers necessary and appropriate to help in the successful operation of the Borrower. This policy applies to all business loan programs, including 504 loans.

§ 120.531 Extension of maturity.

SBA may agree to extend the maturity of a loan for up to 10 years beyond its original maturity if the extension will aid in the orderly repayment of the loan.

§ 120.532 What is a loan Moratorium?

SBA may assume a Borrower's obligation to repay principal and interest on a loan by agreeing to make the payments to the Lender on behalf of the Borrower under terms and conditions set by SBA. This relief is called a ''Moratorium.'' Complete information concerning this program may be obtained from local SBA offices.

§ 120.535 Standards for Lender and CDC loan servicing, loan liquidation and debt collection litigation.

(a) *Service using prudent lending standards.* Lenders and CDCs must service 7(a) and 504 loans in their portfolio no less diligently than their non-SBA portfolio, and in a commercially reasonable manner, consistent with prudent lending standards, and in accordance with Loan Program Requirements. Those Lenders and CDCs that do not maintain a non-SBA loan portfolio must adhere to the same prudent lending standards for loan servicing followed by commercial lenders on loans without a government guarantee.

(b) *Liquidate using prudent lending standards.* Lenders and Authorized CDC Liquidators must liquidate and conduct debt collection litigation for 7(a) and 504 loans in their portfolio no less diligently than for their non-SBA portfolio, and in a prompt, cost-effective and commercially reasonable manner, consistent with prudent lending standards, and in accordance with Loan Program Requirements and with any SBA approval of either a liquidation or litigation plan or any amendment of such a plan. Lenders and CDCs that do not maintain a non-SBA loan portfolio must adhere to the same prudent lending standards followed by commercial lenders that liquidate loans without a government guarantee. They are also to operate in accordance with Loan Program Requirements and with any SBA approval of either a liquidation or litigation plan or any amendment of such a plan.

(c) *Absence of actual or apparent conflict of interest.* A CDC must not take any action in the liquidation or debt collection litigation of a 504 loan that would result in an actual or apparent conflict of interest between the CDC (or any employee of the CDC) and any Third Party Lender, associate of a Third Party Lender, or any person participating in a liquidation, foreclosure or loss mitigation action.

(d) *SBA rights to take over servicing or liquidation.* SBA may, in its sole discretion, undertake the servicing, liquidation and/or litigation of any 7(a) or 504 loan. If SBA elects to service, liquidate and/or litigate a loan, it will notify the relevant Lender or CDC in writing, and, upon receiving such notice, the Lender or CDC must assign the Loan Instruments to SBA and provide any needed assistance to allow SBA to service, liquidate and/or litigate the loan. SBA will notify the Borrower of the change in servicing. SBA may use contractors to perform these actions.

[72 FR 18361, Apr. 12, 2007]

§ 120.536 Servicing and liquidation actions that require the prior written consent of SBA.

(a) *Actions by Lenders and CDCs.* Except as otherwise provided in a Supplemental Guarantee Agreement with a Lender or an Agreement with a CDC, SBA must give its prior written consent before a Lender or CDC takes any of the following actions:

(1) Increases the principal amount of a loan above that authorized by SBA at loan origination.

(2) Confers a Preference on the Lender or CDC or engages in an activity that creates a conflict of interest.

(3) Compromises the principal balance of a loan.

(4) Takes title to any property in the name of SBA.

(5) Takes title to environmentally contaminated property, or takes over operation and control of a business that handles hazardous substances or hazardous wastes.

(6) Transfers, sells or pledges more than 90% of a loan.

(7) Takes any action for which prior written consent is required by a Loan Program Requirement.

(b) *Actions by CDCs only (other than PCLP CDCs).* SBA must give its prior written consent before a CDC, other than a PCLP CDC, takes any of the following actions with respect to a 504 loan:

(1) Alters substantially the terms or conditions of any Loan Instrument.

(2) Releases collateral having a cumulative market value in excess of 10 percent of the Debenture amount or $10,000, whichever is less.

(3) Accelerates the maturity of the note.

(4) Compromises or releases any claim against any Borrower or obligor, or against any guarantor, standby creditor, or any other person that is contingently liable for moneys owed on the loan.

(5) Purchases or pays off any indebtedness secured by the property that serves as collateral for a defaulted 504 loan, such as payment of the debt(s) owed to a lien holder or lien holders with priority over the lien securing the loan.

(6) Accepts a workout plan to restructure the material terms and conditions of a loan that is in default or liquidation.

(7) Takes any action for which prior written consent is required by a Loan Program Requirement.

(c) *Documentation requirements.* For all servicing/liquidation actions not requiring SBA's prior written consent, Lenders and CDCs must document the justifications for their decisions and retain these and supporting documents in their file for future SBA review to determine if the actions taken by the Lender or CDC were prudent, commercially reasonable, and complied with all Loan Program Requirements.

[72 FR 18361, Apr. 12, 2007]

§ 120.540 Liquidation and litigation plans.

(a) *SBA oversight.* SBA may monitor or review liquidation through the review of liquidation plans which all Authorized CDC Liquidators and certain Lenders must submit to SBA for approval prior to undertaking liquidation, and through liquidation wrap-up reports which Lenders must submit to SBA at the completion of liquidation. SBA will monitor debt collection litigation, such as judicial foreclosures, bankruptcy proceedings and other state and federal insolvency proceedings, through the review of litigation plans, as set forth in this section.

(b) *Liquidation plan.* An Authorized CDC Liquidator and a Lender for a loan made under its authority as a CLP Lender must, prior to undertaking any liquidation, submit a written proposed liquidation plan to SBA and receive SBA's written approval of that plan.

(c) *Litigation plan.* An Authorized CDC Liquidator and a Lender must obtain SBA's prior approval of a litigation plan before proceeding with any Non-Routine Litigation, as defined in paragraph (c)(1) of this section. SBA's prior approval is not required for Routine Litigation, as defined in paragraph (c)(2) of this section.

(1) Non-Routine Litigation includes:

(i) All litigation where factual or legal issues are in dispute and require resolution through adjudication;

(ii) Any litigation where legal fees are estimated to exceed $10,000;

(iii) Any litigation involving a loan where a Lender or Authorized CDC Liquidator has an actual or potential conflict of interest with SBA; and

(iv) Any litigation involving a 7(a) or 504 loan where the Lender or CDC has made a separate loan to the same borrower which is not a 7(a) or 504 loan.

(2) Routine Litigation means uncontested litigation, such as non-adversarial matters in bankruptcy and undisputed foreclosure actions, having estimated legal fees not exceeding $10,000.

(d) *Decision by SBA to take over litigation.* If a Lender or Authorized CDC Liquidator is conducting, or proposes to conduct, debt collection litigation on a 7(a) loan or 504 loan, SBA may take over the litigation if SBA determines that the outcome of the litigation could adversely affect SBA's administration of the loan program or that the Government is entitled to legal remedies that are not available to the Lender or Authorized CDC Liquidator. Examples of cases that could adversely affect SBA's administration of a loan program include, but are not limited to, situations where SBA determines that:

(1) The litigation involves important governmental policy or program issues.

(2) The case is potentially of great precedential value or there is a risk of adverse precedent to the Government.

(3) The Lender or Authorized CDC Liquidator has an actual or potential conflict of interest with SBA.

(4) The legal fees of the Lender or Authorized CDC Liquidator's outside counsel are unnecessary, unreasonable or not customary in the locality.

(e) *Amendments to a liquidation or litigation plan.* Lenders and Authorized CDC Liquidators must submit an amended liquidation or litigation plan to address any material changes arising during the course of the liquidation or litigation that were not addressed in the original plan or an amended plan. Lenders and Authorized CDC Liquidators must obtain SBA's written approval of the amended plan prior to taking any further liquidation or litigation action. Examples of such material changes that would require the approval of an amended plan include, but are not limited to:

(1) Changes arising during the course of Routine Litigation that transform the litigation into Non-Routine Litigation, such as when the debtor contests a foreclosure or when the actual legal fees incurred exceed $10,000.

(2) If SBA has approved a litigation plan where anticipated legal fees exceed $10,000, or has approved an amended plan, and thereafter the anticipated or actual legal fees increase by more than 15 percent.

(3) If SBA has approved a liquidation plan, or an amended plan, and thereafter the anticipated or actual costs of conducting the liquidation increase by more than 15 percent.

(f) *Limited waiver of need for a written liquidation or litigation plan.* SBA may, in its discretion, and upon request by a Lender or Authorized CDC Liquidator, waive the requirements of paragraphs (b), (c) or (e) of this section, if one of the following extraordinary circumstances warrant such a waiver: the need for expeditious action to avoid the potential risk of loss on the loan or dissipation of collateral exists; an immediate response is required to litigation by a borrower, guarantor or third party; or another urgent reason arises. The Lender or Authorized CDC Liquidator must obtain SBA's written consent to such waiver before undertaking the Emergency action, if at all practicable. SBA's waiver will apply only to the specific action(s) which the Lender or Authorized CDC Liquidator has identified to SBA as being necessary to address the Emergency. The Lender or Authorized CDC Liquidator must, as soon after the Emergency as is practicable, submit a written liquidation or litigation plan to SBA or, if appropriate, a written amended plan, and may not take further liquidation or litigation action without written approval of such plan or amendment by SBA.

(g) *Appeals.* A Lender for loans made under its authority as a CLP Lender or an Authorized CDC Liquidator that disagrees with an SBA office's decision pertaining to an original or amended liquidation plan, other than such portions of the plan that address litigation matters, may submit a written appeal to the D/FA within 30 days of the decision. The D/FA or designee will make

the final Agency decision in consultation with the Associate General Counsel for Litigation. A Lender or Authorized CDC Liquidator that disagrees with an SBA office's decision pertaining to an original or amended litigation plan, or the portion of a liquidation plan addressing litigation matters, may submit a written appeal to the Associate General Counsel for Litigation within 30 days of the decision. The Associate General Counsel for Litigation will make the final Agency decision in consultation with the D/FA.

[72 FR 18362, Apr. 12, 2007, as amended at 74 FR 45753, Sept. 4, 2009]

§ 120.541 Time for approval by SBA.

(a) Except as set forth in paragraph (c) of this section, in responding to a request for approval under §§ 120.540(b), 120.540(c), 120.536(b)(5) or 120.536(b)(6), SBA will approve or deny the request within 15 business days of the date when SBA receives the request. If SBA is unable to approve or deny the request within this 15-day period, SBA will provide a written notice of no decision to the Lender or Authorized CDC Liquidator, stating the reason for SBA's inability to act; an estimate of the additional time required to act on the plan or request; and, if SBA deems appropriate, requesting additional information.

(b) Except as set forth in paragraph (c) of this section, unless SBA gives its written consent to a proposed liquidation or litigation plan, or a proposed amendment of a plan, or any of the actions set forth in § 120.536(b)(5) or § 120.536(b)(6), SBA will not be deemed to have approved the proposed action.

(c) If a Lender seeks to perform liquidation on a loan made under its authority as a CLP Lender by submitting a liquidation plan to SBA for approval, SBA will approve or deny such plan within ten business days. If SBA fails to approve or deny the plan within ten business days, SBA will be deemed to have approved such plan.

[72 FR 18362, Apr. 12, 2007]

§ 120.542 Payment by SBA of legal fees and other expenses.

(a) *Legal fees SBA will not pay.* (1) SBA will not pay legal fees or other costs that a Lender or Authorized CDC Liquidator incurs:

(i) In asserting a claim, cross claim, counterclaim, or third-party claim against SBA or in defense of an action brought by SBA, unless payment of such fees or costs is otherwise required by federal law.

(ii) In connection with actions of a Lender or Authorized CDC Liquidator's outside counsel for performing non-legal liquidation services, unless authorized by SBA prior to the action.

(iii) In taking actions which solely benefit a Lender or Authorized CDC Liquidator and which do not benefit SBA, as determined by SBA.

(2) SBA will not pay legal fees or other costs a Lender or CDC incurs in the defense of, or pay for any settlement or adverse judgment resulting from, a suit, counterclaim or other claim by a borrower, guarantor, or other party that seeks damages based upon a claim that the Lender or CDC breached any duty or engaged in any wrongful actions, unless SBA expressly directed the Lender or CDC to undertake the allegedly wrongful action that is the subject of the suit, counterclaim or other claim.

(b) *Legal fees SBA may decline to pay.* In addition to any right or authority SBA may have under law or contract, SBA may, in its discretion, decline to pay a Lender or Authorized CDC Liquidator for all, or a portion, of legal fees and/or other costs incurred in connection with the liquidation and/or litigation of a 7(a) loan or 504 loan under any of the following circumstances:

(1) SBA determines that the Lender or Authorized CDC Liquidator failed to perform liquidation or litigation promptly and in accordance with commercially reasonable standards, in a prudent manner, or in accordance with any Loan Program Requirement or SBA approvals of either a liquidation or litigation plan or any amendment of such a plan.

(2) A Lender or Authorized CDC Liquidator fails to obtain prior written approval from SBA for any liquidation or litigation plan, or for any amended liquidation or litigation plan, or for any action set forth in § 120.536, when such approval is required by these regulations or a Loan Program Requirement.

(3) If SBA has not specifically approved fees or costs identified in an original or amended liquidation or litigation plan under §120.540, and SBA determines that such fees or costs are not reasonable, customary or necessary in the locality in question. In such cases, SBA will pay only such fees as it deems are necessary, customary and reasonable in the locality in question.

(c) *Fees for liquidation actions performed by Authorized CDC Liquidators.* Subject to paragraph (d) of this section, SBA will compensate Authorized CDC Liquidators for their liquidation actions on 504 loans, whether such actions are performed by the CDC or the CDC's contractor retained in accordance with §120.975(a)(2) or (b)(2)(ii). The compensation fee will be a percentage (to be published in the FEDERAL REGISTER from time to time, but not to exceed 10%) of the net recovery proceeds realized from the sale of collateral or other liquidation actions on an individual loan, up to a fee of $25,000 for such loan, and a lower percentage (also to be published in the FEDERAL REGISTER from time to time, but not to exceed 5%) of the realized net recovery proceeds above such amounts. The compensation fee limits set forth in this paragraph (c) do not include reasonable, customary and necessary administrative costs related to liquidation activities on such loan that are incurred in accordance with the liquidation plan, or amendments thereto, approved by SBA pursuant to §120.540(b). The Authorized CDC Liquidator may compensate its contractor up to the amount it receives from SBA. All requests for compensation fees must be received by SBA within nine months from the date of SBA's purchase of the defaulted debenture. Fee requests not received within such timeframe will be automatically rejected.

(d) *Appeals—liquidation costs.* A Lender or Authorized CDC Liquidator that disagrees with a decision by an SBA office to decline to reimburse all, or a portion, of the fees and/or costs incurred in conducting liquidation may appeal this decision in writing to the D/FA within 30 days of the decision. The decision of the D/FA or designee will be made in consultation with the Associate General Counsel for Litigation, and will be the final Agency decision.

(e) *Appeals—litigation costs.* A Lender or Authorized CDC Liquidator that disagrees with a decision by SBA to decline to reimburse all, or a portion, of the legal fees and/or costs incurred in conducting debt collection litigation may appeal this decision in writing to the Associate General Counsel for Litigation within 30 days of the decision. The decision of the Associate General Counsel for Litigation will be made in consultation with the D/FA, and will be the final Agency decision.

[72 FR 18362, Apr. 12, 2007, as amended at 74 FR 45753, Sept. 4, 2009]

§120.545 What are SBA's policies concerning the liquidation of collateral and the sale of business loans and physical disaster assistance loans, physical disaster business loans and economic injury disaster loans?

(a) *Liquidation policy.* SBA or the Lender may liquidate collateral securing a loan if the loan is in default or there is no reasonable prospect that the loan can be repaid within a reasonable period.

(b) *Sale and conversion of loans.* Without the consent of the Borrower, SBA may:

(1) Sell a direct loan;

(2) Convert a guaranteed or immediate participation loan to a direct loan; or

(3) Convert an immediate participation loan to a guaranteed loan or a loan owned solely by the Lender.

(4) Sell direct and purchased 7(a) and 501, 502, 503 and 504 loans and physical disaster home loans, physical disaster business loans and economic injury disaster loans in asset sales. SBA will offer these loans for sale to qualified bidders by means of competitive procedures at publicly advertised sales. Bidder qualifications will be set for each sale in accordance with the terms and conditions of each sale.

(c) *Disposal of collateral and assets acquired through foreclosure or conveyance.* SBA or the Lender may sell real and personal property (including contracts and claims) pledged to secure a loan that is in default in accordance with the provisions of the related security

instrument (*see* §120.550 for Homestead Protection for Farmers).

(1) *Competitive bids or negotiated sales.* Generally, SBA will offer loan collateral and acquired assets for public sale through competitive bids at auctions or sealed bid sales. The Lender may use negotiated sales if consistent with its usual practice for similar non-SBA assets.

(2) *Lease of acquired property.* Normally, neither SBA nor a Lender will rent or lease acquired property or grant options to purchase. SBA and the Lender will consider proposals for a lease if it appears a property cannot be sold advantageously and the lease may be terminated on reasonable notice upon receipt of a favorable purchase offer.

(d) *Recoveries and security interests shared.* SBA and the Lender will share pro rata (in accordance with their respective interests in a loan) all loan payments or recoveries, including proceeds from asset sales, all reasonable expenses (including advances for the care, preservation, and maintenance of collateral securing the loan and the payment of senior lienholders), and any security interest or guarantee (excluding SBA's guarantee) which the Lender or SBA may hold or receive in connection with a loan.

(e) *Guarantors.* Guarantors of financial assistance have no rights of contribution against SBA on an SBA guaranteed or direct loan. SBA is not deemed to be a co-guarantor with any other guarantors.

[61 FR 3235, Jan. 31, 1996, as amended at 64 FR 44110, Aug. 13, 1999; 65 FR 17133, Mar. 31, 2000; 68 FR 51680, Aug. 28, 2003. Redesignated and amended at 72 FR 18362, Apr. 12, 2007]

§120.546 Loan asset sales.

(a) *General.* Loan asset sales are governed by §120.545(b)(4) and by this section.

(b) *7(a) loans*—(1) *For loans approved on or after May 14, 2007.* The Lender will be deemed to have consented to SBA's sale of the loan (guaranteed and unguaranteed portions) in an asset sale conducted or overseen by SBA upon the occurrence any of the following:

(i) SBA's purchase of the guaranteed portion of the loan from the Registered Holder for a loan where the guaranteed portion has been sold in the Secondary Market pursuant to subpart F of this part and after default, the Lender has not exercised its option to purchase such guaranteed portion; or

(ii) SBA's purchase of the guaranteed portion from the Lender, provided however, that if SBA purchased the guaranteed portion pursuant to §120.520(a)(1) prior to the Lender's completion of liquidation for the loan, then SBA will not sell such loan in an asset sale until nine months from the date of SBA's purchase; or

(iii) SBA receives written consent from the Lender.

(2) For loans identified in paragraph (b)(1)(i) of this section, the Lender may request that SBA withhold the loan from an asset sale if the Lender submits a written request to SBA within 15 business days of SBA's purchase of the guaranteed portion of the loan from the Registered Holder and if such request addresses the issues described in this subparagraph. The Lender's written request must advise SBA of the status of the loan, the Lender's plans for workout and/or liquidation, including and pending sale of loan collateral or foreclosure proceedings arranged prior to SBA's purchase that already are underway, and the Lender's estimated schedule for restructuring the loan or liquidating the collateral. SBA will consider the Lender's request and, based on the circumstances, SBA in its sole discretion may elect to defer including the loan in an asset sale in order to provide the Lender additional time to complete the planned restructuring and/or liquidation actions.

(3) *For loans approved before May 14, 2007.* SBA must obtain written consent from the Lender for the sale of such loans in an asset sale.

(4) After SBA has purchased the guaranteed portion of a loan from the Registered Holder or from the Lender, the Lender must continue to perform all necessary servicing and liquidation actions for the loan up to the point the loan is transferred to the purchaser in an asset sale. The Lender also must cooperate and take all necessary actions to effectuate both the asset sale and the transfer of the loan to the purchaser in the asset sale.

(c) *504 loans*—(1) *PCLP Loans.* After SBA's purchase of a Debenture, SBA may at its sole discretion sell a defaulted PCLP Loan in an asset sale conducted or overseen by SBA, after providing to the PCLP CDC that made the loan advance notice of not less than 90 days before the date upon which SBA first makes its records concerning such loan available to prospective purchasers for examination.

(2) *All other 504 loans.* After SBA's purchase of a Debenture, SBA may at its sole discretion sell a defaulted 504 loan in an asset sale conducted or overseen by SBA.

[72 FR 18364, Apr. 12, 2007]

HOMESTEAD PROTECTION FOR FARMERS

§ 120.550 What is homestead protection for farmers?

SBA may lease to a farmer-Borrower the farm residence occupied by the Borrower and a reasonable amount of adjoining property (no more than 10 acres and seven farm buildings), if they were acquired by SBA as a result of a defaulted farm loan made or guaranteed by SBA (*see* the Consolidated Farm and Rural Development Act, 7 U.S.C. 1921, for qualifying loan purposes).

§ 120.551 Who is eligible for homestead protection?

SBA must notify the Borrower in possession of the availability of these homestead protection rights within 30 days after SBA acquires the property. A farmer-Borrower must:

(a) Apply for the homestead occupancy to the SBA field office which serviced the loan within 90 days after SBA acquires the property;

(b) Provide evidence that the farm produces farm income reasonable for the area and economic conditions;

(c) Show that at least 60 percent of the Borrower and spouse's gross annual income came from farm or ranch operations in at least any two out of the last six calendar years;

(d) Have resided on the property during the previous six years; and

(e) Be personally liable for the debt.

§ 120.552 Lease.

If approved, the applicant must personally occupy the residence during the term of the lease and pay a reasonable rent to SBA. The lease will be for a period of at least 3 years, but no more than 5 years. A lease of less than 5 years may be renewed, but not beyond 5 years from the original lease date. During or at the end of the lease period, the lessee has a right of first refusal to reacquire the homestead property under terms and conditions no less favorable than those offered to any other purchaser.

§ 120.553 Appeal.

If the application is denied, the Borrower may appeal the decision to the D/FA. Until the conclusion of any appeal, the Borrower may retain possession of the homestead property.

§ 120.554 Conflict of laws.

In the event of a conflict between the homestead provisions at §§ 120.550 through 120.553 of this part, and any state law relating to the right of a Borrower to designate for separate sale or to redeem part or all of the real property securing a loan foreclosed by the Lender, state law shall prevail.

Subpart F—Secondary Market

FISCAL AND TRANSFER AGENT (FTA)

§ 120.600 Definitions.

(a) *Certificate* is the document the FTA issues representing either a beneficial fractional undivided interest in a Pool (Pool Certificate), or a fractional undivided interest in some or all of the guaranteed portion of an individual 7(a) guaranteed loan (Individual Certificate).

(b) *Current* means that no repayment from a Borrower to a Lender is over 29 days late measured from the due date of the payment on the records of the FTA's central registry (Pools) or the entity servicing the loan (individual guaranteed portion).

(c) *Dollar-Weighted Average Net Rate* of a Pool is calculated by multiplying the interest rate of each loan in the Pool by the ratio of that loan's current outstanding guaranteed principal to

the current outstanding guaranteed principal of all loans in the Pool, and adding the sum of the resulting products. The Dollar-Weighted Average Net Rate of a Pool will fluctuate over the life of the Pool as loan defaults, prepayments and normal loan repayments occur.

(d) *FTA* is the SBA's fiscal and transfer agent.

(e) *Note Rate* is the interest rate on the Borrower's note.

(f) *Net Rate* is the interest rate on an individual guaranteed portion of a loan in a Pool.

(g) *Pool* is an aggregation of SBA guaranteed portions of loans made by Lenders.

(h) *Pool Assembler* is a financial institution that:

(1) Organizes and packages a Pool by acquiring the SBA guaranteed portions of loans from Lenders;

(2) Resells fractional interests in the Pool to Registered Holders; and

(3) Directs the FTA to issue Certificates.

(i) *Pool Rate* is the interest rate on a Pool Certificate.

(j) *Registered Holder* is the Certificate owner listed in FTA's records.

(k) *SBA's Secondary Market Program Guide* is an issuance from SBA which describes the characteristics of Secondary Market transactions.

(l) *Weighted Average Coupon (WAC) Pool* is a Pool where the interest rate payable to the investor is equal to the Dollar-Weighted Average Net Rate of the Pool.

[61 FR 3235, Jan. 31, 1996, as amended at 73 FR 67102, Nov. 13, 2008; 76 FR 63546, Oct. 12, 2011]

§ 120.601 SBA Secondary Market.

The SBA secondary market (''Secondary Market'') consists of the sale of Certificates, representing either a fractional undivided interest in some or all of the guaranteed portion of an individual 7(a) guaranteed loan or a fractional undivided interest in a Pool consisting of the SBA guaranteed portions of a number of 7(a) guaranteed loans. Transactions involving interests in Pools or the sale of individual guaranteed portions of loans are governed by the contracts entered into by the parties, SBA's Secondary Market Program Guide, and this subpart. See sections 5(f), (g), and (h) of the Small Business Act (15 U.S.C. 634(f), (g), and (h)).

[76 FR 63546, Oct. 12, 2011]

CERTIFICATES

§ 120.610 Form and terms of Certificates.

(a) *General form and content.* Each Certificate must be registered with the FTA. SBA must approve the terms of the Certificate.

(b) *Face amount of Pool Certificate.* The face amount of a Pool Certificate cannot be less than a minimum amount as specified in the Program Guide, and the dollar amount of Certificates must be in increments which SBA will specify in the Program Guide (except for one Certificate in each Pool). SBA may change these requirements based upon an analysis of market conditions and program experience, and will publish any such change in the FEDERAL REGISTER.

(c) *Basis of payment for Pool Certificates.* Principal installments and interest payments are based on the unpaid principal balance of the portion of the Pool represented by a Pool Certificate. All prepayments on loans in the Pool must be passed through to the appropriate Registered Holders with the regularly scheduled payments to such Holders.

(d) *Basis of payment for Individual Certificates.* Principal installments and interest payments are based on the unpaid principal balance of the SBA guaranteed portion of the loan supporting an Individual Certificate. The Certificate must provide for a pass through to the Registered Holder of payments which the FTA receives from a Lender or any entity servicing the loan, less applicable fees.

(e) *Interest rate on Pool Certificate.* The interest rate on a Pool Certificate will be either the lowest Net Rate of any individual guaranteed portion of a loan in the Pool or the Dollar-Weighted Average Net Rate of the Pool.

[61 FR 3235, Jan. 31, 1996, as amended at 73 FR 67102, Nov. 13, 2008]

§ 120.611 Pools backing Pool Certificates.

(a) *Pool characteristics.* As set forth in the Program Guide, each Pool must have:

(1) A minimum number of guaranteed portions of loans;

(2) A minimum aggregate principal balance of the guaranteed portions;

(3) A maximum percentage of the Pool which an individual guaranteed portion may constitute;

(4) A maximum allowable difference between the highest and lowest note interest rates;

(5) A maximum allowable difference between the remaining terms to maturity of the loans in the Pool;

(6) A minimum weighted average maturity at Pool formation; and

(7) A maximum allowable difference between the highest and lowest Net Rate on the guaranteed portions that are placed in a WAC Pool.

(b) *Adjustment of Pool characteristics.* SBA may adjust the Pool characteristics periodically based upon program experience and market conditions.

(c) *Increments of guaranteed portion.* If the amount of the guaranteed portion of an individual 7(a) guaranteed loan is more than $500,000, a Pool Assembler may elect to divide the guaranteed portion into increments of $500,000 and one increment of any remaining amount less than $500,000, in order to permit the maximum amount of any guaranteed portion in a Pool to be not more than $500,000. Only one increment from a loan to a specific borrower may be included in a Pool.

[61 FR 3235, Jan. 31, 1996, as amended at 73 FR 67102, Nov. 13, 2008; 76 FR 63546, Oct. 12, 2011]

§ 120.612 Loans eligible to back Certificates.

(a) Pool Certificates are backed by the SBA guaranteed portions of loans comprising the Pool. An Individual Certificate is backed by the SBA guaranteed portion of a single loan. Any such loan must:

(1) Be current as of the date the Pool is formed or the individual guaranteed portion of a loan is initially sold in the Secondary Market;

(2) Be guaranteed under the Act; and

(3) Meet such other standards as SBA may determine to be necessary for the successful operation of the Secondary Market program.

(b) The loans that back a Pool must meet the SBA requirements in effect at the time the Pool is formed.

§ 120.613 Secondary Participation Guarantee Agreement.

When a Lender wants to sell the guaranteed portion of a loan, it enters into a Secondary Participation Guarantee Agreement (''SPGA'') with SBA and the prospective purchaser. The terms of sale between the Lender and the purchaser cannot require the Lender or SBA to repurchase the guaranteed portion of the loan except in accordance with the terms of the SPGA. Before execution of the SPGA, the Lender must:

(a) Submit to FTA a copy of the proposed SPGA, the note, and such other documents as SBA may require;

(b) Except for export working capital loans, disburse to the Borrower the full amount of the loan; and

(c) Pay SBA all guarantee fees relevant to the loan in full.

[61 FR 3235, Jan. 31, 1996, as amended at 68 FR 51680, Aug. 28, 2003]

THE SBA GUARANTEE OF A CERTIFICATE

§ 120.620 SBA guarantee of a Pool Certificate.

(a) *Extent of Guarantee.* SBA guarantees to a Registered Holder the timely payment of principal and interest installments and any prepayment or other recovery of principal to which the Registered Holder is entitled. If the Borrower of a loan in a Pool backing the Certificates does not make a required installment payment, SBA, through the FTA, will make advances to maintain the schedule of interest and principal payments to the Registered Holders.

(b) *SBA guarantee backed by full faith and credit.* SBA's guarantee of the Pool Certificate is backed by the full faith and credit of the United States.

§ 120.621 SBA guarantee of an Individual Certificate.

(a) *Extent of SBA guarantee.* With respect to Individual Certificates, SBA

guarantees to purchase from the Registered Holder the guaranteed portion of the loan for an amount equal to the unpaid principal and accrued interest due as of the date of SBA's purchase, less deductions for applicable fees. Unlike the SBA guarantee with respect to pooled loans, SBA does not guarantee timely payment on Individual Certificates.

(b) *What triggers the SBA guarantee.* SBA's guarantee to the Registered Holder may be called upon when:

(1) The Borrower remains in uncured default for 60 days on payments of principal or interest due on the note;

(2) The Lender fails to send to the FTA on a timely basis payments it received from the Borrower; or

(3) The FTA fails to send to the Registered Holder on a timely basis any payments it has received from the Lender.

(c) *Full faith and credit.* SBA's guarantee to the Registered Holder is backed by the full faith and credit of the United States.

POOL ASSEMBLERS

§ 120.630 Qualifications to be a Pool Assembler.

(a) *Application to become Pool Assembler.* The application to become a Pool Assembler is available from the D/FA. In order to qualify as a Pool Assembler, an entity must send the application to the D/FA, with an application fee, and certify that it:

(1) Is regulated by the appropriate agency as defined in section 3(a)(34)(G) of the Securities Exchange Act of 1934 (15 U.S.C. 78c(a)(34)(G));

(2) Meets all financial and other applicable requirements of its regulatory authority and the Government Securities Act of 1986, as amended (Pub. L. 99–571, 100 Stat. 3208);

(3) Has the financial capability to assemble acceptable and eligible guaranteed loan portions in sufficient quantity to support the issuance of Pool Certificates; and

(4) Is in good standing with SBA (as the D/FA determines in his or her discretion), and is Satisfactory with the Office of the Comptroller of the Currency (''OCC'') if it is a national bank, the Federal Deposit Insurance Corporation if it is a bank not regulated by the OCC, or the Financial Industry Regulatory Authority (''FINRA'') if it is a member as determined by SBA.

(5) For any pool assembler that is an SBA Lender, that the SBA 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, 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) *Approval by SBA.* An entity may not submit Pool applications to the FTA until SBA has approved the application to become a Pool Assembler.

(c) *Conduct of business by Pool Assembler.* An entity continues to qualify as a Pool Assembler so long as it:

(1) Meets the eligibility standards in paragraph (a) of this section;

(2) Conducts its business in accordance with SBA regulations and accepted securities or banking industry practices, ethics, and standards; and

(3) Maintains its books and records in accordance with generally accepted accounting principles or in accordance with the guidelines of the regulatory body governing its activities.

[61 FR 3235, Jan. 31, 1996, as amended at 73 FR 75517, Dec. 11, 2008; 82 FR 39503, Aug. 21, 2017]

§ 120.631 Suspension or termination of Pool Assembler.

(a) *Suspension or termination.* The D/FA may suspend a Pool Assembler from operating in the Secondary Market for up to 18 months or terminate its status as a Pool Assembler, if the Pool Assembler (and/or its Associates):

(1) Does not comply with any of the requirements in § 120.630 (a) and (c);

(2) Has been indicted or otherwise formally charged with, or convicted of, a misdemeanor or felony;

(3) Has received an adverse civil judgment that it has committed a breach of

trust or a violation of a law or regulation protecting the integrity of business transactions or relationships;

(4) Has not formed a Pool for at least three years; or

(5) Is under investigation by its regulating authority for activities which may affect its fitness to participate in the Secondary Market.

(b) *Suspension procedures.* The D/FA shall notify a Pool Assembler by certified mail, return receipt requested, of the decision to suspend and the reasons therefore at least 10 business days prior to the effective date of the suspension. The Pool Assembler may appeal the suspension made under this section pursuant to the procedures set forth in part 134 of this chapter. The action of the D/FA shall remain in effect pending resolution of the appeal.

(c) *Notice of termination.* In order to terminate a Pool Assembler, the D/FA must issue an order to show cause why the SBA should not terminate the Pool Assembler's participation in the Secondary Market. The Pool Assembler may appeal the termination made under this section pursuant to procedures set forth in part 134 of this chapter. The action of the D/FA shall remain in effect pending resolution of the appeal.

MISCELLANEOUS PROVISIONS

§ 120.640 Administration of the Pool and Individual Certificates.

(a) *FTA responsibility.* The FTA has the responsibility to administer each Pool or Individual Certificate. It shall maintain a registry of Registered Holders and other information as SBA requires.

(b) *Self-liquidating.* Each Pool or individual guaranteed portion of a loan in the Secondary Market is self-liquidating because of Borrower payments or prepayments, redemption by SBA, and/or payments by SBA or the Lender after default by the Borrower. Substitution of the guaranteed portions of existing loans for defaulted loans is not permitted.

(c) *SBA's right to subrogation.* If SBA pays a claim under a guarantee with respect to a Certificate issued under this subpart, it must be subrogated fully to the rights satisfied by such payment.

(d) *SBA ownership rights not limited.* No Federal, State or local law can preclude or limit the exercise by SBA of its ownership rights in the portions of loans constituting the Pool against which the Certificates are issued.

§ 120.641 Disclosure to purchasers.

(a) *Information to purchaser.* Prior to any sale, the Pool Assembler, Registered Holder of an Individual Certificate, or any subsequent seller must disclose to the purchaser, verbally or in writing, information on the terms, conditions, and yield as described in the SBA Secondary Market Program Guide.

(b) *Information on transfer document.* The seller must provide the same information described in paragraph (a) of this section in writing on the transfer document when the seller submits it to the FTA. After the sale of an Individual Certificate, the FTA will provide the disclosure information in writing to the purchaser.

(c) *Information in prospectus.* If the Registered Holder is a trust, investment Pool, mutual fund or other security, it must disclose the information in paragraph (a) of this section to investors through a prospectus and other promotional material if an Individual Certificate or Pool Certificate is placed into or used as the backing for the investment vehicle.

§ 120.642 Requirements before the FTA issues Pool Certificates.

Before the FTA issues any Pool Certificate, the Pool Assembler must deliver to it the following documents:

(a) A properly completed Pool application form;

(b) Either:

(1) Individual Certificates evidencing the guaranteed portions comprising the Pool; or

(2) An executed SPGA and related documentation for the loans whose guaranteed portions are to be part of the Pool; and

(c) Any other documentation which SBA may require.

§ 120.643 Requirements before the FTA issues Individual Certificates.

(a) *FTA issuance of initial Certificate.* Before the FTA can issue the Individual Certificate for a guaranteed portion of a loan, the original seller must provide the following documents to the FTA:

(1) An executed SPGA;

(2) A copy of the note representing the guaranteed loan; and

(3) Any other documentation which SBA may require.

(b) Review of documentation. SBA may review or require the FTA to review any documentation before the FTA issues a Certificate.

§ 120.644 Transfers of Certificates.

(a) *General rule.* Certificates are transferable. Transfers in the Secondary Market must comply with Article 8 of the Uniform Commercial Code of the State of New York. The seller must use the detached form of assignment (SBA Form 1088), unless the seller and purchaser choose to use another form which the SBA approves. The FTA may refuse to issue a Certificate until it is satisfied that the documents of transfer are complete.

(b) *Transfer on FTA records.* In order for the transfer of a Certificate to be effective the FTA must reflect it on its records.

(c) *Contents of letter of transmittal accompanying the transfer of Certificates.* (1) A letter of transmittal must accompany each Certificate which a Registered Holder submits to the FTA for transfer. The Registered Holder must supply the following information in the letter:

(i) Pool number, if applicable;

(ii) Certificate number;

(iii) Name of purchaser of Certificate;

(iv) Address and tax identification number of the purchaser;

(v) Name and telephone number of the person handling or facilitating the transfer;

(vi) Instructions for the delivery of the new Certificate.

(2) The Registered Holder must also send the fee which the FTA charges for this service. The FTA will supply fee information to the Registered Holder.

(d) *Lender cannot purchase guaranteed portion of loan it made.* The Lender (or its Associate) that made a 7(a) guaranteed loan cannot purchase the guaranteed portion of that loan in the Secondary Market. If a Lender does purchase the guaranteed portion of one of its own loans, it shall not have the unconditional guarantee of SBA.

§ 120.645 Redemption of Certificates.

(a) *Redemption of Individual Certificate.* The prepayment of the underlying loan or a default on such loan will trigger the redemption of the Certificate by FTA/SBA in accordance with the procedures prescribed in the SPGA.

(b) *Redemption of Pool Certificate.* The FTA and SBA may redeem a Pool Certificate because of prepayment or default of all loans in a Pool.

§ 120.650 Registration duties of FTA in Secondary Market.

The FTA registers all Certificates. This means it issues, transfers title to, and redeems them. All financial transactions relating to a guaranteed portion of a loan flow through the FTA. In fulfilling its obligation to keep the central registry current, the FTA may, with SBA's approval, obtain any necessary information from the parties involved in the Secondary Market.

§ 120.651 Claim to FTA by Registered Holder to replace Certificate.

(a) To replace a Certificate because of loss, theft, destruction, mutilation, or defacement, the Registered Holder must:

(1) Give the FTA information about the Certificate and the facts relating to the claim;

(2) File an indemnity bond acceptable to SBA and the FTA with a surety to protect the interests of SBA and the FTA;

(3) Pay the FTA its fee to replace a Certificate; and

(4) Use an affidavit of loss (form available from the FTA) to report:

(i) The name and address of the Registered Holder (and the name and capacity of any representative actually filing the claim);

(ii) The Certificate by Pool number, if applicable;

(iii) The Certificate number;

(iv) The original principal amount;

(v) The name in which the Certificate was registered;

(vi) Any assignment, endorsement or other writing on the Certificate; and

(vii) A statement of the circumstances of the theft or loss.

(b) When the FTA receives notice of the theft or loss, it will stop any transfer of the Certificate. The Registered Holder must send to the FTA all available portions of a mutilated or defaced Certificate. When the Registered Holder completes these steps, the FTA will replace the Certificate.

§ 120.652 FTA fees.

The FTA may charge reasonable servicing fees, transfer fees, and other fees as the SBA and FTA may negotiate under contract.

SUSPENSION OR REVOCATION OF PARTICIPANT IN SECONDARY MARKET

§ 120.660 Suspension or revocation.

(a) *Temporary suspension or revocation of Lender, broker, dealer, or Registered Holder for violation of Secondary Market rules and regulations or other risks to SBA.* The D/FA together with the Director, Office of Credit Risk Management (D/OCRM) may suspend for a period of no more than 120 calendar days or revoke for a period of no more than two (2) years, the privilege of a Lender, broker, dealer, or Registered Holder to sell, purchase, broker, or deal in loans or Certificates for:

(1) Committing a serious violation, in SBA's discretion, of:

(i) The regulations governing the Secondary Market; or

(ii) Any provisions in the contracts entered into by the parties, including SBA Forms 1086, 1088 and 1454;

(2) Knowingly submitting false or fraudulent information to the SBA or FTA; or

(3) A Lender's receipt, from its primary Federal or state regulator (including SBA), of a cease and desist order, a consent agreement affecting capital or commercial lending issues, a supervisory action citing unsafe or unsound banking practices, or any other supervisory action a primary regulator establishes hereafter that addresses unsafe or unsound lending practices; or a going concern opinion issued by the Lender's auditor. A Lender subject to a public action or going concern opinion must notify the D/FA and the D/OCRM within five (5) business days (or as soon as practicable thereafter) of the public issuance of any such action or the issuance of a going concern opinion. The Lender notice shall include copies of all relevant documents for SBA review.

(b) *Additional rules for suspension or revocation of broker or dealer.* In addition to acting under paragraph (a) of this section, the D/FA may suspend or revoke the privilege of any broker or dealer to sell or otherwise deal in Certificates in the Secondary Market if:

(1) Its supervisory agency has revoked or suspended the broker or dealer from engaging in the securities business, or is investigating the firm or broker for a practice which SBA considers, in its sole discretion, to be relevant to the broker's or dealer's fitness to participate in the Secondary Market;

(2) The broker or dealer has been indicted or otherwise formally charged with a misdemeanor or felony which bears on its fitness to participate in the Secondary Market; or

(3) A civil judgment is entered holding that the broker or dealer has committed a breach of trust or a violation of any law or regulation protecting the integrity of business transactions or relationships.

(c) *Notice to suspend or revoke.* The D/FA and the D/OCRM shall notify the affected party in writing, providing the reasons therefore, at least 10 business days prior to the effective date of the suspension or revocation. The affected party may appeal the suspension or revocation made under this section pursuant to the procedures set forth in part 134 of this chapter. The action taken by the D/FA and the D/OCRM will remain in effect pending resolution of the appeal.

(d) *Early termination of suspension or revocation.* SBA may, by written notice, terminate a Secondary Market suspension or revocation under this section, if the D/FA and the D/OCRM, in their sole discretion, determine that such termination is warranted for good cause.

[61 FR 3235, Jan. 31, 1996, as amended at 82 FR 39503, Aug. 21, 2017]

Subpart G—Microloan Program

§ 120.700 What is the Microloan Program?

The Microloan Program assists women, low income individuals, minority entrepreneurs, and other small businesses which need small amounts of financial assistance. Under this program, SBA makes direct and guaranteed loans to Intermediaries (as defined below) who use the proceeds to make loans to eligible borrowers. SBA may also make grants under the program to Intermediaries and other qualified nonprofit entities to be used for marketing, management, and technical assistance to the program's target population.

[61 FR 3235, Jan. 31, 1996, as amended at 66 FR 47073, Sept. 11, 2001]

§ 120.701 Definitions.

(a) *Deposit account* is a demand, time, savings, passbook, or similar account maintained with an insured depository institution (not including an account evidenced by a Certificate of Deposit).

(b) *Grant* is a Federal award of money, or property in lieu of money (including cooperative agreements) to an eligible grantee that must account for its use. The term does not include the provision of technical assistance, revenue sharing, loans, loan guarantees, interest subsidies, insurance, direct appropriations, or any fellowship or other lump sum award.

(c) *Insured depository institution* means any Federally insured bank, savings association, or credit union.

(d) *Intermediary* is an entity participating in the Microloan Program which makes and services Microloans to eligible small businesses and which provides marketing, management, and technical assistance to its borrowers. It may be:

(1) A private, nonprofit community development corporation or other entity;

(2) A consortium of private, nonprofit community development corporations or other entities;

(3) A quasi-governmental economic development entity, other than a state, county, municipal government or any agency thereof; or

(4) An agency of or a nonprofit entity established by a Native American Tribal Government.

(e) *Microloan* is a short-term, fixed interest rate loan of not more than $50,000 made by an Intermediary to an eligible small business.

(f) *Non-Federal sources* are sources of funds other than the Federal Government and may include indirect costs or in-kind contributions paid for under non-Federal programs. Community Block Development Grants are considered non-Federal sources.

(g) *Non-lending technical assistance provider* (NTAP) is an entity which receives grant funds from SBA to provide technical assistance to Microloan borrowers.

(h) *Specialized Intermediary* is an Intermediary which maintains a portfolio of Microloans averaging $10,000 or less.

[61 FR 3235, Jan. 31, 1996, as amended at 66 FR 47073, Sept. 11, 2001; 66 FR 47878, Sept. 14, 2001; 76 FR 63546, Oct. 12, 2011; 80 FR 34046, June 15, 2015]

§ 120.702 Are there limitations on who can be an Intermediary or on where an Intermediary may operate?

(a) *Prior experience requirement.* To be eligible to be an Intermediary, an organization must:

(1) Have made and serviced short-term fixed rate loans of not more than $50,000 to newly established or growing small businesses for at least one year: and

(2) Have at least one year of experience providing technical assistance to its borrowers.

(b) *Limitation to one state.* An Intermediary may not operate in more than one state unless the appropriate Office of Capital Access official in accordance with Delegations of Authority determines that it would be in the best interests of the small business community for it to operate across state lines.

[61 FR 3235, Jan. 31, 1996, as amended at 66 FR 47878, Sept. 14, 2001; 73 FR 75517, Dec. 11, 2008; 76 FR 63546, Oct. 12, 2011]

§ 120.703 How does an organization apply to become an Intermediary?

(a) *Application Process.* Organizations interested in becoming Intermediaries

should contact SBA for information on the application process.

(b) *Documentation in support of application.* The application must include a detailed narrative statement describing:

(1) The types of businesses assisted in the past and those the applicant intends to assist with Microloans;

(2) The average size of the loans made in the past and the average size of intended Microloans;

(3) The extent to which the applicant will make Microloans to small businesses in rural areas;

(4) The geographic area in which the applicant intends to operate, including a description of the economic and demographic conditions existing in the intended area of operations;

(5) The availability and cost of obtaining credit for small businesses in the area;

(6) The applicant's experience and qualifications in providing marketing, management, and technical assistance to small businesses; and

(7) Any plan to use other technical assistance resources (such as counselors from the Service Corps of Retired Executives) to help Microloan borrowers.

§ 120.704 How are applications evaluated?

(a) *Evaluation criteria.* In selecting Intermediaries, SBA will attempt to insure that Microloans are available to small businesses in all industries and particularly to small businesses located in urban and rural areas.

(b) *Preference for organizations which make very small loans.* In selecting Intermediaries, SBA will give priority to applicants which maintain a portfolio of loans averaging $10,000 or less.

(c) *Consideration of quasi-governmental organizations.* Generally, SBA will consider applications by quasi-governmental organizations only when it determines that program services for a particular geographic area would be best provided by such organization.

[61 FR 3235, Jan. 31, 1996, as amended at 66 FR 47878, Sept. 14, 2001]

§ 120.705 What is a Specialized Intermediary?

At the end of an Intermediary's first year of participation in the program, SBA will determine whether it qualifies as a Specialized Intermediary. An Intermediary qualifies as a Specialized Intermediary if it maintains a portfolio of Microloans averaging $10,000 or less. Specialized Intermediaries qualify for more favorable interest rates on SBA loans. If, after the first year, an Intermediary qualifies as a Specialized Intermediary, the special interest rate is applied retroactively to SBA loans made to the Intermediary. After the first year SBA will determine an Intermediary's qualifications as a Specialized Intermediary annually, based on its lending practices during the term of its participation in the program. Specialized Intermediaries also qualify for a greater amount of technical assistance grant funding.

[61 FR 3235, Jan. 31, 1996, as amended at 66 FR 47878, Sept. 14, 2001]

§ 120.706 What are the terms and conditions of an SBA loan to an Intermediary?

(a) *Loan Amount.* An Intermediary may not borrow more than $750,000 in the first year of participation in the program. In later years, the Intermediary's obligation to SBA may not exceed an aggregate of $5 million, subject to statutory limitations on the total amount of funds available per state.

(b) *Repayment terms.* During the first year of the loan, an Intermediary is not required to make any payments, but interest accrues from the date that SBA disburses the loan proceeds to the Intermediary. After that, SBA will determine the periodic payments. The loan must be repaid within 10 years.

(c) *Interest rate.* The interest rate is equal to the rate applicable to five-year obligations of the United States Treasury, adjusted to the nearest one-eighth percent, less 1.25 percent. However, the interest rate for Specialized Intermediaries is equal to the rate applicable to five-year obligations of the United States Treasury, adjusted to the nearest one-eighth percent, less two percent.

(d) *Collateral.* As security for repayment of the SBA loan, an Intermediary must pledge to SBA a first lien position in the MRF (described below), LLRF (described below), and all notes receivable from Microloans.

(e) *Default.* If for any reason an Intermediary is unable to make payment to SBA when due, SBA may accelerate maturity of the loan and demand payment in full. In this event, or if an Intermediary violates this part or the terms of its loan agreement, it must surrender possession of all collateral described in paragraph (d) of this section to SBA. The Intermediary is not obligated to pay SBA any loss or deficiency which may remain after liquidation of the collateral unless the loss was caused by fraud, negligence, violation of any of the ethical requirements of §120.140, or violation of any other provision of this part.

(f) *Fees.* SBA does not charge Intermediaries any fees for loans under this Program. An Intermediary may, however, pay minimal closing costs to third parties, such as filing and recording fees.

[61 FR 3235, Jan. 31, 1996, as amended at 66 FR 47073, Sept. 11, 2001; 76 FR 63546, Oct. 12, 2011]

§ 120.707 What conditions apply to loans by Intermediaries to Microloan borrowers?

(a) Except as otherwise provided in this paragraph, an Intermediary may only make Microloans to small businesses eligible to receive financial assistance under this part. A borrower may also use Microloan proceeds to establish a nonprofit child care business. An Intermediary may also make Microloans to businesses with an Associate who is currently on probation or parole; provided, however, that the Associate is not on probation or parole for an offense involving fraud or dishonesty or, in the case of a child care business, is not on probation or parole for an offense against children. Proceeds from Microloans may be used only for working capital and acquisition of materials, supplies, furniture, fixtures, and equipment. SBA does not review Microloans for creditworthiness.

(b) *Amount and maturity.* Generally, Intermediaries should not make a Microloan of more than $10,000 to any borrower. An Intermediary may not make a Microloan of more than $20,000 unless the borrower demonstrates that it is unable to obtain credit elsewhere at comparable interest rates and that it has good prospects for success. An Intermediary may not make a Microloan of more than $50,000, and no borrower may owe an Intermediary more than $50,000 at any one time. Each Microloan must be repaid within six years.

(c) *Interest rate.* The maximum interest rate that can be charged a Microloan borrower is:

(1) On loans of more than $10,000, the interest rate charged on the SBA loan to the Intermediary, plus 7.75 percentage points; and

(2) On loans of $10,000 or less, the interest rate charged on the SBA loan to the Intermediary, plus 8.5 percentage points.

[61 FR 3235, Jan. 31, 1996, as amended at 66 FR 47073, Sept. 11, 2001; 66 FR 47878, Sept. 14, 2001; 76 FR 63547, Oct. 12, 2011; 80 FR 34046, June 15, 2015]

§ 120.708 What is the Intermediary's financial contribution?

The Intermediary must contribute from non-Federal sources an amount equal to 15 percent of any loan that it receives from SBA. The contribution may not be borrowed. For purposes of this program, Community Development Block Grants are considered non-Federal sources.

§ 120.709 What is the Microloan Revolving Fund?

The Microloan Revolving Fund (''MRF'') is a Deposit Account into which an Intermediary must deposit the proceeds from SBA loans, its contributions from non-Federal sources, and payments from its Microloan borrowers. An Intermediary may only withdraw from this account the money needed to establish the Loan Loss Reserve Fund (§120.710), proceeds for each Microloan it makes, and any payments to be made to SBA.

[61 FR 3235, Jan. 31, 1996, as amended at 80 FR 34046, June 15, 2015]

§ 120.710 What is the Loan Loss Reserve Fund?

(a) *General.* The Loan Loss Reserve Fund (''LLRF'') is a Deposit Account which an Intermediary must establish to pay any shortage in the MRF caused by delinquencies or losses on Microloans.

(b) *Level of Loan Loss Reserve Fund.* Until it is in the Microloan program for at least five years, an Intermediary must maintain a balance on deposit in its LLRF equal to 15 percent of the outstanding balance of the notes receivable owed to it by its Microloan borrowers (''Portfolio'').

(c) *SBA review of Loan Loss Reserve Fund.* After an Intermediary has been in the Microloan program for five years, it may request SBA's appropriate Office of Capital Access official in accordance with Delegations of Authority to reduce the percentage of its Portfolio which it must maintain in its LLRF to an amount equal to the actual average loan loss rate during the preceding five-year period. Upon receipt of such request, he/she will review the Intermediary's annual loss rate for the most recent five-year period preceding the request.

(d) *Reduction of Loan Loss Reserve Fund.* The appropriate Office of Capital Access official in accordance with Delegations of Authority has the authority to reduce the percentage of an Intermediary's Portfolio that it must maintain in its LLRF to an amount equal to the actual average loan loss rate during the preceding five-year period. The appropriate Office of Capital Access official in accordance with Delegations of Authority cannot reduce the LLRF to less than ten percent of the Portfolio.

(e) *What must an intermediary demonstrate to get a reduction in Loan Loss Reserve Fund?* To receive a reduction in its LLRF, an Intermediary must:

(1) Have satisfactory SBA performance, as determined by SBA in its discretion. The Intermediary's Risk Rating, among other factors, will be considered in determining satisfactory SBA performance. Other factors may include, but are not limited to, 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

(2) No other factors exist that may impair the Intermediary's ability to repay all obligations which it owes to the SBA under the Microloan program.

[61 FR 3235, Jan. 31, 1996, as amended at 65 FR 17439, Apr. 3, 2000; 73 FR 75517, Dec. 11, 2008; 80 FR 34046, June 15, 2015; 82 FR 39504, Aug. 21, 2017]

§ 120.711 What rules govern Intermediaries?

Intermediaries must operate in accordance with applicable statutes, regulations, policy notices, SBA's Standard Operating Procedures (SOPs), and the information in the application.

§ 120.712 How does an Intermediary get a grant to assist Microloan borrowers?

(a) *General.* An Intermediary is eligible to receive grant funding from SBA of not more than 25 percent of the outstanding balance of all SBA loans to the Intermediary. The Intermediary must contribute, solely from non-Federal sources, an amount equal to 25 percent of the grant. Contributions may be made in cash or in kind.

(b) *Limitations on grant funds.* An Intermediary may not borrow its contribution. It may only use grant funds to provide Microloan borrowers with marketing, management, and technical assistance, except that:

(1) Up to 25 percent of the grant funds may be used to provide information and technical assistance to prospective Microloan borrowers; and

(2) Grant monies may be used to attend training required by SBA.

(c) *Intermediaries eligible to receive additional grant monies.* An Intermediary may receive an additional SBA grant equal to five percent of the outstanding balance of all loans received from SBA (with no obligation to contribute additional matching funds) if the Intermediary is a Specialized Intermediary.

(d) *Third party contracts for technical assistance.* An Intermediary may use no more than 25 percent of the grant funds it receives from SBA for contracts with third parties for the latter to provide

technical assistance to Microloan borrowers.

[61 FR 3235, Jan. 31, 1996, as amended at 66 FR 47073, Sept. 11, 2001; 76 FR 63547, Oct. 12, 2011; 80 FR 34047, June 15, 2015]

§ 120.713 Does SBA provide technical assistance to Intermediaries?

SBA may procure technical assistance for an Intermediary to improve its knowledge, skill, and understanding of microlending by awarding a grant to a more experienced Intermediary. SBA may also obtain such assistance for prospective Intermediaries in areas of the country that are either not served or underserved by an existing Intermediary.

§ 120.714 How are grants made to non-lending technical assistance providers (NTAP)?

SBA selects non-lending technical assistance providers (NTAP) to receive grant funds for technical assistance to Microloan borrowers.

(a) *Grant procedure for non-Intermediaries.* Any nonprofit entity that is not an Intermediary may apply to SBA for a grant to provide marketing, management and technical assistance to low-income individuals for the purpose of assisting them in obtaining private sector financing in amounts of $50,000 or less. To qualify, it must submit information regarding its ability to provide this assistance. If approved, the grant agreement will establish the terms and conditions for the grant.

(b) *Number and amount of grants.* In each year of the Microloan Program, SBA may make no more than 55 grants to non-Intermediaries for terms of up to five years. A grant may not exceed $200,000.

(c) *Contribution by nonprofit entity.* The nonprofit entity must contribute an amount equal to 20 percent of the grant. The contribution from the nonprofit entity must come solely from non-Federal sources, and may include direct costs or in-kind contributions paid for under non-Federal programs.

[61 FR 3235, Jan. 31, 1996, as amended at 66 FR 47073, Sept. 11, 2001; 66 FR 47878, Sept. 14, 2001; 76 FR 63547, Oct. 12, 2011]

§ 120.715 Does SBA guarantee any loans an Intermediary obtains from another source?

(a) SBA may guarantee not less than 90 percent of loans made by for-profit or nonprofit entities (or an alliance of such entities) to no more than 10 Intermediaries in urban areas and 10 Intermediaries in Rural Areas (as defined in § 120.10).

(b) Any loan guaranteed by SBA under this section will have a term of 10 years. If an Intermediary receives such a loan, it will not need to repay any principal or interest during the first year, although the interest will accrue. During the second through fifth years, the Intermediary will pay interest only. During the sixth through tenth years, it will pay interest and fully amortize the principal.

(c) The interest rate on any loan under this section shall be calculated as described in § 120.706.

[61 FR 3235, Jan. 31, 1996, as amended at 66 FR 47073, Sept. 11, 2001]

§ 120.716 What is the minimum number of loans an Intermediary must make each Federal fiscal year?

(a) *Minimum loan requirement.* Intermediaries must close and fund the required number of microloans per year (October 1–September 30) as follows, except that an Intermediary entering the program will not be required to meet the minimum in that year:

(1) For fiscal year 2015, four microloans,

(2) For fiscal year 2016, six microloans,

(3) For fiscal year 2017, eight microloans, and

(4) For fiscal years 2018 and thereafter, ten microloans per year.

(b) Intermediaries that do not meet the minimum loan requirement are not eligible to receive new grant funding unless they submit a corrective action plan acceptable to SBA, in its discretion. Intermediaries that have submitted acceptable corrective action plans may receive a reduced grant at SBA's discretion.

[80 FR 34047, June 15, 2015]

Subpart H—Development Company Loan Program (504)

§ 120.800 The purpose of the 504 program.

As authorized by Congress, SBA has established this program to foster economic development, create or preserve job opportunities, and stimulate growth, expansion, and modernization of small businesses.

§ 120.801 How a 504 Project is financed.

(a) One or more small businesses may apply for 504 financing through a CDC serving the area where the 504 Project is located. SBA issues an Authorization if it agrees to guarantee part of the funding for a Project.

(b) Usually, a Project requires interim financing from an interim lender (often the same lender that later provides a portion of the permanent financing).

(c) Generally, permanent financing of the Project consists of:

(1) A contribution by the small business in an amount of at least 10 percent of the Project costs;

(2) A loan made with the proceeds of a CDC Debenture for up to 40 percent of the Project costs and certain administrative costs, collateralized by a second lien on the Project Property; and

(3) A *Third Party Loan* comprising the balance of the financing, collateralized by a first lien on the Project property (see § 120.920).

(d) The Debenture is guaranteed 100 percent by SBA (with the full faith and credit of the United States), and sold to Underwriters who form Debenture Pools. Investors purchase interests in Debenture Pools and receive Certificates representing ownership of all or part of a Debenture Pool. SBA and CDCs use various agents to facilitate the sale and service of the Certificates and the orderly flow of funds among the parties.

[61 FR 3235, Jan. 31, 1996, as amended at 64 FR 2118, Jan. 13, 1999]

§ 120.802 Definitions.

The following terms have the same meaning wherever they are used in this subpart. Defined terms are capitalized wherever they appear.

Area of Operations is the geographic area where SBA has approved a CDC's request to provide 504 program services to small businesses on a permanent basis. The minimum Area of Operations is the State in which the CDC is incorporated.

Central Servicing Agent (CSA) is an entity that receives and disburses funds among the various parties involved in 504 financing under a master servicing agent agreement with SBA.

Certificate is a document issued by SBA or its agent representing ownership of all or part of a Debenture Pool.

Debenture is an obligation issued by a CDC and guaranteed 100 percent by SBA, the proceeds of which are used to fund a 504 loan.

Debenture Pool is an aggregation of Debentures.

Designated Attorney is the CDC closing attorney that SBA has approved to close loans under an expedited closing process for a Priority CDC.

Investor is an owner of a beneficial interest in a Debenture Pool.

Job Opportunity is a full time (or equivalent) permanent job created within two years of receipt of 504 funds, or retained in the community because of a 504 loan.

Lead SBA Office is the SBA District Office designated by SBA as the primary liaison between SBA and a CDC and with responsibility for managing SBA's relationship with that CDC.

Local Economic Area is an area, as determined by SBA, that is in a State other than the State in which an existing CDC (or an applicant applying to become a CDC) is incorporated, is contiguous to the CDC's existing Area of Operations (or the applicant's proposed Area of Operations) of its State of incorporation, and is a part of a local trade area that is contiguous to the CDC's Area of Operations (or applicant's proposed Area of Operations) of its State of incorporation. Examples of a local trade area would be a city that is bisected by a State line or a metropolitan statistical area that is bisected by a State line.

Multi-State CDC is a CDC that is incorporated in one State and is authorized by SBA to operate as a CDC in a

State contiguous to its State of incorporation beyond any contiguous Local Economic Areas.

Net Debenture Proceeds are the portion of Debenture proceeds that finance eligible Project costs (excluding administrative costs).

Priority CDC is a CDC certified to participate on a permanent basis in the 504 program (see § 120.812) that SBA has approved to participate in an expedited 504 loan and Debenture closing process.

Project is the purchase or lease, and/or improvement or renovation of long-term fixed assets by a small business, with 504 financing, for use in its business operations.

Project Property is one or more long-term fixed assets, such as land, buildings, machinery, and equipment, acquired or improved by a small business, with 504 financing, for use in its business operations.

Third Party Loan is a loan from a commercial or private lender, investor, or Federal (non-SBA), State or local government source that is part of the Project financing.

Underwriter is an entity approved by SBA to form Debenture Pools and arrange for the sale of Certificates.

[61 FR 3235, Jan. 31, 1996, as amended at 64 FR 2118, Jan. 13, 1999; 65 FR 42632, July 11, 2000; 68 FR 57980, Oct. 7, 2003]

CERTIFICATION PROCEDURES TO BECOME A CDC

§ 120.810 Applications for certification as a CDC.

(a) An applicant for certification as a CDC must apply to the SBA District Office serving the jurisdiction in which the applicant has or proposes to locate its headquarters (see § 101.103 of this chapter).

(b) The applicant must apply for an Area of Operations. The applicant's proposed Area of Operations must include the entire State in which the applicant is incorporated, and may include Local Economic Areas. An applicant may not apply to cover an area as a Multi-State CDC.

(c) The applicant must demonstrate that it satisfies the CDC certification and operational requirements in §§ 120.820, and 120.822 through 120.824. The applicant also must include an operating budget, approved by the applicant's Board of Directors, which demonstrates the required financial ability (as described in § 120.825), and a plan to meet CDC operational requirements (without specializing in a particular industry) in §§ 120.821, and 120.826 through 120.830.

(d) The District Office will forward the application and its recommendation to the D/FA, who will make the final decision. SBA will notify the CDC in writing of its decision, and, if the petition is declined, the reasons for the decision.

[68 FR 57980, Oct. 7, 2003]

§ 120.812 Probationary period for newly certified CDCs.

(a) Newly certified CDCs will be on probation for a period of two years from the date of certification, at the end of which the CDC must petition the Lead SBA Office for:

(1) Permanent CDC status; or

(2) A single, one-year extension of probation.

(b) SBA will consider the failure to file a petition before the end of the probationary period as a withdrawal from the 504 program. If the CDC elects withdrawal, SBA will direct the CDC to transfer all funded and/or approved loans to another CDC, SBA, or another servicer approved by SBA.

(c) The Lead SBA Office will send the petition and its recommendation to the D/FA, who will make the final decision. SBA will determine permanent CDC status or an extension of probation, in part, based upon the CDC's compliance with the certification and operational requirements in §§ 120.820 through 120.830. To be considered for permanent CDC status or an extension of probation, the CDC must have satisfactory SBA performance, as determined by SBA in its discretion. The CDC's Risk Rating, among other factors, will be considered in determining satisfactory SBA performance. Other factors may include, but are not limited to, review/examination assessments, historical performance measures, loan volume to the extent that it impacts performance measures, and other performance related measurements and information (such as contribution toward SBA mission).

(d) SBA will notify the CDC in writing of its decision, and, if the petition is declined, the reasons for the decision.

[68 FR 57980, Oct. 7, 2003, as amended at 73 FR 75517, Dec. 11, 2008; 82 FR 39504, Aug. 21, 2017]

REQUIREMENTS FOR CDC CERTIFICATION AND OPERATION

§ 120.816 CDC non-profit status and good standing.

A CDC must be a non-profit corporation, except that for-profit CDCs certified by SBA prior to January 1, 1987 may retain their certifications. An SBIC may not become a CDC. A CDC must be in good standing based upon the following criteria:

(a) In good standing in the State in which the CDC is incorporated and any other State in which the CDC conducts business.

(b) In compliance with all laws, including taxation requirements, in the State in which the CDC is incorporated and any other State in which the CDC conducts business.

(c) Must have satisfactory SBA performance, as determined by SBA in its discretion. The CDC's Risk Rating, among other factors, will be considered in determining satisfactory SBA performance. Other factors may include, but are not limited to, review/examination assessments, historical performance measures, loan volume to the extent that it impacts performance measures, and other performance related measurements and information (such as contribution toward SBA mission).

[68 FR 57980, Oct. 7, 2003, as amended at 73 FR 75518, Dec. 11, 2008. Redesignated at 79 FR 15649, Mar. 21, 2014; 82 FR 39504, Aug. 21, 2017]

EFFECTIVE DATE NOTE: At 84 FR 66294, Dec. 4, 2019, §120.816 was amended by adding paragraph (d), effective Jan. 3, 2020. For the convenience of the user, the added text is set forth as follows:

§ 120.816 CDC non-profit status and good standing.

* * * * *

(d) If a non-profit CDC has a membership and the members are responsible for electing or appointing voting directors to the CDC's Board of Directors, no person or entity can control more than 25 percent of the CDC's voting membership.

§ 120.818 Applicability to existing for-profit CDCs.

Unless expressly provided otherwise in the regulations, any Loan Program Requirement that applies to non-profit CDCs also applies to for-profit CDCs.

[79 FR 15649, Mar. 21, 2014]

EFFECTIVE DATE NOTE: At 84 FR 66294, Dec. 4, 2019, §120.818 was amended by designating the undesignated paragraph as paragraph (a) and adding paragraph (b), effective Jan. 3, 2020. For the convenience of the user, the added text is set forth as follows:

§ 120.818 Applicability to existing for-profit CDCs.

* * * * *

(b) No person or entity can own or control more than 25 percent of a for-profit CDC's stock.

§ 120.820 CDC Affiliation.

(a) A CDC must be independent and must not be affiliated (as determined in accordance with §121.103 of this chapter) with any Person (as defined in §120.10) except as permitted under this section.

(b) A CDC may be affiliated with an entity (other than a 7(a) Lender or another CDC) whose function is economic development in the same Area of Operations and that is either a non-profit entity or a State or local government or political subdivision (e.g., council of governments).

(c) A CDC must not be affiliated (as determined in accordance with §121.103) with or invest, directly or indirectly, in a 7(a) Lender. A CDC that was affiliated with a 7(a) Lender as of November 6, 2003 may continue such affiliation.

(d) A CDC must not be affiliated (as determined in accordance with §121.103 of this chapter) with another CDC. In addition, a CDC must not directly or indirectly invest in or finance another CDC, except with the prior written approval of D/FA or designee and D/OCRM or designee if they determine in their discretion that such approval is in the best interests of the 504 Loan Program.

(e) A CDC may remain affiliated with a for-profit entity (other than a 7(a) Lender) if such affiliation existed prior to March 21, 2014. A CDC may also be affiliated with a for-profit entity

(other than a 7(a) Lender) whose function is economic development in the same Area of Operations with the prior written approval of the D/FA or designee if he or she determines in his or her discretion that such approval is in the best interests of the 504 Loan Program.

(f) A CDC must not directly or indirectly invest in a Licensee (as defined in §107.50 of this chapter) licensed by SBA under the SBIC program authorized in Part A of Title III of the Small Business Investment Act, 15 U.S.C. 681 et seq. A CDC that has an SBA-approved investment in a Licensee as of November 6, 2003 may retain such investment.

[79 FR 15649, Mar. 21, 2014]

§ 120.821 CDC Area of Operations.

A CDC must operate only within its designated Area of Operations approved by SBA except as provided in §120.839.

[68 FR 57980, Oct. 7, 2003]

§ 120.823 CDC Board of Directors.

(a) The CDC, whether for-profit or nonprofit, must have a Board of Directors with at least nine (9) voting directors. A CDC may request the approval of the D/FA or designee to have a Board with fewer directors than 9 for good cause. SBA recommends that the CDC create a Board with no more than 25 voting directors. The Board must be actively involved in encouraging economic development in the Area of Operations. The initial Board may be created by any method permitted by applicable State law. At a minimum, the Board must have directors with background and expertise in internal controls, financial risk management, commercial lending, legal issues relating to commercial lending, and corporate governance. Directors may be either currently employed or retired. A CDC must have at least one voting director that represents the economic, community or workforce development fields, and at least two voting directors that represent the commercial lending field.

(b) At least two voting members of the Board of Directors, other than the CDC manager, must possess commercial lending experience satisfactory to SBA. When the Board votes on SBA loan approval or servicing actions, at least two voting Board members, with such commercial lending experience, other than the CDC manager, must be present and vote.

(c) The Board of Directors must meet at least quarterly and shall be responsible for the actions of the CDC and any committees established by the Board of Directors. In addition, the Board of Directors is subject to the following requirements:

(1) Except for the CDC manager, no person on the CDC's staff may be a voting director of the Board;

(2) A quorum must be present to transact business. The quorum shall be set by the CDC but shall be no less than 50% of the voting members of the Board of Directors;

(3) Attendance at meetings may be through any format permitted by State law;

(4) Directors from the commercial lending fields must comprise less than 50% of the representation on the Board; and

(5) No CDC Board member may serve on the Board of another CDC.

(d) The Board shall have and exercise all corporate powers and authority and be responsible for all corporate actions and business. There must be no actual or appearance of a conflict of interest with respect to any actions of the Board. The Board is responsible for ensuring that the structure and operation of the CDC, as set forth in the Bylaws, comply with SBA's Loan Program Requirements. The responsibilities of the Board include, but are not limited, to the following:

(1) Approving the mission and the policies for the CDC;

(2) Hiring, firing, supervising and annually evaluating the CDC manager;

(3) Setting the salary for the CDC manager and reviewing all salaries;

(4) Establishing committees, at its discretion, including the following:

(i) *Executive Committee*. To the extent authorized in the Bylaws, the Board of Directors may establish an Executive Committee. The Executive Committee may exercise the authority of the Board; however, the delegation of its authority does not relieve the Board of its responsibility imposed by law or

Loan Program Requirements. No further delegation or redelegation of this authority is permitted. If the Board establishes an Executive Committee and delegates any of its authority to the Executive Committee as set forth in the Bylaws of the CDC, the Executive Committee must:

(A) Be chosen by and from the Board of Directors from the Board; and

(B) Meet the same organizational and representational requirements as the Board of Directors, except that the Executive Committee must have a minimum of five voting members who must be present to conduct business.

(ii) *Loan Committee.* The Board of Directors may establish a Loan Committee. The Loan Committee may exercise the authority of the Board only as set forth below; however, the delegation of its authority does not relieve the Board of its responsibility imposed by law or Loan Program Requirements. If the Board of Directors chooses to establish a Loan Committee, no CDC staff or manager may serve on the Loan Committee. The Loan Committee must:

(A) Be chosen by the Board of Directors, and consist of individuals with a background in either financial risk management, commercial lending, or legal issues relating to commercial lending who are not associated with another CDC;

(B) Have a Quorum of at least five (5) Loan Committee members authorized to vote;

(C) Have at least two (2) Loan Committee members with commercial lending experience satisfactory to SBA;

(D) Have no actual or appearance of a conflict of interest, including for example, a Loan Committee member participating in deliberations on a loan for which the Third Party Lender is the member's employer or the member is otherwise associated with the Third Party Lender; and

(E) Consist of Loan Committee members who live or work in the Area of Operations of the State where the 504 project they are voting on is located unless the project falls under one of the exceptions listed in § 120.839.

(5) Ensuring that the CDC's expenses are reasonable and customary;

(6) Hiring directly an independent auditor to provide the financial statements in accordance with Loan Program Requirements;

(7) Monitoring the CDC's portfolio performance on a regular basis;

(8) Reviewing a semiannual report on portfolio performance from the CDC manager, which would include, but not be limited to, asset quality and industry concentration;

(9) Ensuring that the CDC establishes and maintains adequate reserves for operations;

(10) Ensuring that the CDC invests in economic development in each of the States in its Area of Operations in which it has a portfolio, and approving each investment. If the investment is included in the CDC's budget, the Board's approval of the budget may be deemed approval of the investment. If the investment is not included in the budget, the Board must separately approve the investment;

(11) Establishing a policy in the Bylaws of the CDC prohibiting an actual conflict of interest or the appearance of same, and enforcing such policy (see § 120.140 and § 120.851);

(12) Retaining accountability for all of the actions of the CDC;

(13) Establishing written internal control policies, in accordance with § 120.826;

(14) Establishing commercially reasonable loan approval policies, procedures, and standards. The Bylaws must include any delegations of authority to the Loan Committee and Executive Committee, if either Committee has been established. In addition, the CDC must establish and set forth in detail in a policy manual its credit approval process. All 504 loan applications must have credit approval prior to submission to the Agency. The Loan Committee, if established, may be delegated the authority to provide credit approval for loans up to $2,000,000 but, for loans of $1,000,000 to $2,000,000, the Loan Committee's action must be ratified by the Board or Executive Committee prior to Debenture closing. Only the Board or Executive Committee, if authorized by the Board, may provide credit approval for loans greater than $2,000,000.

(15) All members of the Board of Directors must annually certify in writing that they have read and understand this section, and copies of the certification must be included in the Annual Report to SBA.

(e) The Board of Directors shall maintain Directors' and Officers' Liability and Errors and Omissions insurance in amounts established by SBA that are based on the size of the CDC's portfolio and other relevant factors.

[79 FR 15649, Mar. 21, 2014, as amended at 82 FR 39504, Aug. 21, 2017]

EFFECTIVE DATE NOTE: At 84 FR 66294, Dec. 4, 2019, §120.823 was amended by revising paragraph (a); removing paragraph (c)(4) and redesignating paragraph (c)(5) as paragraph (c)(4); removing ''five'' and adding ''four'' in its place in paragraph (d)(4)(i)(B); removing ''five (5)'' and adding ''four'' in its place in paragraph (d)(4)(ii)(B), and revising paragraph (d)(4)(ii)(E), effective Jan. 3, 2020. For the convenience of the user, the revised text is set forth as follows:

§ 120.823 CDC Board of Directors.

(a) The CDC, whether for-profit or nonprofit, must have a Board of Directors with at least seven (7) voting directors who live or work in the CDC's State of incorporation or in an area that is contiguous to that State that meets the definition of a Local Economic Area for the CDC. The Board must be actively involved in encouraging economic development in the Area of Operations. The initial Board may be created by any method permitted by applicable State law. At a minimum, the Board must have directors with background and expertise in internal controls, financial risk management, commercial lending, legal issues relating to commercial lending, corporate governance, and economic, community or workforce development. Directors may be either currently employed or retired.

* * * * *

(d) * * *

(4) * * *

(ii) * * *

(E) Consist only of Loan Committee members who live or work in the CDC's State of incorporation or in an area that meets the definition of a Local Economic Area for the CDC, except that, for Projects that are financed under a CDC's Multi-State authority, the CDC must satisfy the requirements of either §120.835(c)(1) or (2) when voting on that Project.

* * * * *

§ 120.824 Professional management and staff.

A CDC must have full-time professional management, including an Executive Director (or the equivalent) managing daily operations. It must also have a full-time professional staff qualified by training and experience to market the 504 Program, package and process loan applications, close loans, service, and, if authorized by SBA, liquidate the loan portfolio, and sustain a sufficient level of service and activity in the Area of Operations. CDCs may obtain, under written contract, management, marketing, packaging, processing, closing, servicing or liquidation services provided by qualified individuals and entities under the following circumstances:

(a) The CDC must have at least one salaried professional employee that is employed directly (not a contractor or an Associate of a contractor) full-time to manage the CDC. The CDC manager must be hired by the CDC's board of directors and subject to termination only by the board. A CDC may petition SBA to waive the requirement of the manager being employed directly if:

(1) Another non-profit entity that has the economic development of the CDC's Area of Operations as one of its principal activities will contribute the management of the CDC, and the management contributed by the other entity also may work on and operate that entity's economic development programs, but must be available to small businesses interested in the 504 program and to 504 loan borrowers during regular business hours; or

(2) The CDC petitioning SBA for such waiver is rural; has insufficient loan volume to justify having management employed directly by the CDC; and has contracted with another CDC located in the same general area to provide the management.

(b) SBA must pre-approve contracts the CDC makes for managing, marketing, packaging, processing, closing, servicing, or liquidation functions. (CDCs may contract for legal and accounting services without SBA approval, except for legal services in connection with loan liquidation or litigation.)

(c) Contracts must clearly identify terms and conditions satisfactory to SBA that permit the CDC to terminate the contract prior to its expiration date on a reasonable basis.

(d) The CDC must provide copies of these contracts to SBA for review annually.

(e) If a CDC's Board believes that it is in the best interest of the CDC to contract for a management, marketing, packaging, processing, closing, servicing or liquidation function, the CDC's Board must explain its reasoning to SBA. The CDC's Board must demonstrate to SBA that:

(1) The compensation under the contract is only from the CDC, reasonable and customary for similar services in the Area of Operations, and is only for actual services performed;

(2) The full term of the contract (including options) is reasonable; and

(3) The contract does not evidence any actual or apparent conflict of interest or self-dealing on the part of any of the CDC's officers, management, and staff, including members of the Board and any Loan Committee.

(f) No contractor (under this section) or Associate of a contractor may be a voting or non-voting member of the CDC's Board.

[65 FR 42632, July 11, 2000, as amended at 68 FR 57981, Oct. 7, 2003]

EFFECTIVE DATE NOTE: At 84 FR 66294, Dec. 4, 2019, §120.824 was revised, effective Jan. 3, 2020. For the convenience of the user, the revised text is set forth as follows:

§ 120.824 Professional management and staff, and contracts for services.

(a) *Management.* A CDC must have full-time professional management, including an executive director or the equivalent (CDC manager) to manage daily operations. This requirement is met if the CDC has at least one salaried professional employee that is employed directly (not a contractor or an officer, director, 20 percent or more equity owner, or key employee of a contractor) on a full-time basis to manage the CDC. The CDC manager must be hired by the CDC's Board of Directors and subject to termination only by the Board. A CDC may obtain, under a written contract, management services provided by a qualified individual under the following circumstances:

(1) The CDC must submit a request for the D/FA (or designee) to approve, in consultation with the D/OCRM (or designee), a waiver of the requirement that the manager be employed directly by the CDC. In its request, the CDC must demonstrate that:

(i) Another non-profit entity (that is not a CDC) that has the economic development of the CDC's Area of Operations as one of its principal activities will provide management services to the CDC and, if the manager is also performing services for the non-profit entity, the manager will be available to small businesses interested in the 504 program and to 504 loan borrowers during regular business hours; or

(ii) The CDC submitting the request for the waiver is rural, has insufficient loan volume to justify having management employed directly by the CDC, and is requesting to contract with another CDC located in the same general area to provide the management.

(2) The CDC must submit a request for the D/FA (or designee), in consultation with the D/OCRM (or designee), to pre-approve the contract for management services. This contract must comply with paragraphs (c)(2) through (4) and, if applicable, paragraph (d) of this section.

(b) *Professional staff.* The CDC must have a full-time professional staff qualified by training and experience to market the 504 Loan Program, package and process loan applications, close loans, service, and, if authorized by SBA, liquidate the loan portfolio, and to sustain a sufficient level of service and activity in the Area of Operations.

(c) *Professional services contracts.* Through a written contract with qualified individuals or entities, a CDC may obtain services for marketing, packaging, processing, closing, servicing, or liquidation functions, or for other services (*e.g.*, legal, accounting, information technology, independent loan reviews, and payroll and employee benefits), provided that:

(1) The contract must be pre-approved by the D/FA (or designee), subject to the following exceptions:

(i) CDCs may contract for legal, accounting, and information technology services without SBA approval, except for legal services in connection with loan liquidation or litigation.

(ii) CDCs may contract for independent loan review services with non-CDC entities without SBA approval. Contracts between CDCs for independent loan reviews must be pre-approved by SBA in accordance with paragraph (d) of this section.

(2) If the contract requires SBA's prior approval under paragraph (c)(1) of this section, the CDC's Board must explain to SBA why it is in the best interest of the CDC to obtain services through a contract and must demonstrate that:

(i) The compensation under the contract is paid only by the CDC obtaining the services, is reasonable and customary for similar services in the Area of Operations, and is only for actual services performed;

(ii) The full term of the contract (including options) is necessary and appropriate and the contract permits the CDC procuring the services to terminate the contract prior to its expiration date with or without cause; and

(iii) There is no actual or apparent conflict of interest or self-dealing on the part of any of the CDC's officers, management, or staff, including members of the Board and Loan Committee, in the negotiation, approval or implementation of the contract.

(3) Neither the contractor nor any officer, director, 20 percent or more equity owner, or key employee of a contractor may be a voting or non-voting member of the CDC's Board.

(4) The CDC procuring the services must provide a copy of all executed contracts requiring SBA prior approval to SBA as part of the CDC's Annual Report submitted under §120.830(a) unless the CDC certifies that it has previously submitted an identical copy of the executed contract to SBA.

(5) With respect to any contract under which the CDC's staff are deemed co-employees of both the CDC and the contractor (*e.g.*, contracts with professional employer organizations to obtain employee benefits, such as retirement and health benefits, for the CDC's staff), the contract must provide that the CDC retains the final authority to hire and fire the CDC's employees.

(6) If the contract is between CDCs, the CDCs and the contract must also comply with paragraph (d) of this section.

(d) *Professional Services Contracts between CDCs.* Notwithstanding the prohibition in 13 CFR 120.820(d) against a CDC affiliating with another CDC, a CDC may obtain services through a written contract with another CDC for managing, marketing, packaging, processing, closing, servicing, independent loan review, or liquidation functions, provided that:

(1) The contract between the CDCs must be pre-approved by the D/FA (or designee), in consultation with the D/OCRM (or designee), who determines in his or her discretion that such approval is in the best interests of the 504 Loan Program and that the terms and conditions of the contract are satisfactory to SBA. For management services, a CDC may contract with another CDC only in accordance with paragraph (a)(1)(ii) of this section.

(2) Except for contracts for liquidation services and independent loan reviews:

(i) The CDCs entering into the contract must be located in the same SBA Region or, if not located in the same SBA Region, must be located in contiguous States. For purposes of this provision, the location of a CDC is the CDC's State of incorporation;

(ii) A CDC may provide assistance to only one CDC per State; and

(iii) No CDC may provide assistance to another CDC in its State of incorporation or in any State in which it has Multi-State authority.

(3) The Board of Directors for each CDC entering into the contract must be separate and independent and may not include any common directors. In addition, if either of the CDCs is for-profit, neither CDC may own any stock in the other CDC. The CDCs are also prohibited from comingling any funds.

(4) With respect to contracts for independent loan reviews, CDCs may not review each other's portfolios or exchange any other services, nor may they enter into any other arrangement with each other that could appear to bias the outcome or integrity of the independent loan review.

(5) The contract must satisfy the requirements set forth in paragraphs (c)(2) through (4) of this section.

§ 120.825 Financial ability to operate.

A CDC must be able to sustain its operations continuously, with reliable sources of funds (such as income from services rendered and contributions from government or other sponsors). Any funds generated from 503 and 504 loan activity by a CDC remaining after payment of staff and overhead expenses must be retained by the CDC as a reserve for future operations or for investment in other local economic development activity in its Area of Operations. If a CDC is operating as a Multi-State CDC, it must maintain a separate accounting for each State of all 504 fee income and expenses and provide, upon SBA's request, evidence that the funds resulting from its Multi-State CDC operations are being invested in economic development activities in each State in which they were generated.

[65 FR 42633, July 11, 2000]

§ 120.826 Basic requirements for operating a CDC.

A CDC must operate in accordance with the following requirements:

(a) *In general.* CDCs must meet all 504 Loan Program Requirements. In its Area of Operations, a CDC must market the 504 program, package and process 504 loan applications, close and service 504 loans, and if authorized by SBA, liquidate and litigate 504 loans. It must supply to SBA current and accurate information about all certification and operational requirements, and maintain the records and submit all reports required by SBA.

(b) *Operations and internal controls.* Each CDC's board of directors must adopt an internal control policy which provides adequate direction to the institution for effective control over and accountability for operations, programs, and resources. The board adopted internal control policy must, at a minimum:

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

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

(3) Direct the operation of a program to review and assess the CDC's 504-related loans. For the 504 review program, the internal control policies must specify the following:

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

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

(iii) Specific control requirements for the CDC's oversight of Lender Service Providers; and

(iv) Standards for training to implement the loan review program; and

(4) Address other control requirements as may be established by SBA.

(c) *Annual Audited/Reviewed Financial Statements.* Each CDC with a 504 loan portfolio balance of $20 million or more (as calculated by SBA) must have its financial statements audited annually by a certified public accountant that is independent and 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). The auditor must be independent, as defined by the AICPA, of the CDC. Annually, the auditor must issue an opinion as to the fairness of the CDC's financial statements and their compliance with GAAP. For CDCs with a 504 portfolio balance of less than $20 million (as calculated by SBA), the CDC's annual financial statements submitted to SBA must be reviewed by an independent CPA in accordance with GAAP.

(d) *Auditor qualifications.* The audit or review must be conducted by an independent certified public accountant who:

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

(2) Agrees in the engagement letter with the CDC 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.

[73 FR 75518, Dec. 11, 2008]

EFFECTIVE DATE NOTE: At 84 FR 66295, Dec. 4, 2019, §120.826(c) was amended by removing the term ''$20 million'' wherever it appeared and adding the term ''$30 million'' in its place; and removing the period at the end of the last sentence and adding '', except that the D/OCRM may require a CDC with a portfolio balance of less than $30 million to submit an audited financial statement in the event the D/OCRM determines, in his or her discretion, that such audit is necessary or appropriate when the CDC is in material noncompliance with Loan Program Requirements.'', effective Jan. 3, 2020.

§120.827 Other services a CDC may provide to small businesses.

A CDC may provide a small business with assistance unrelated to the 504 loan program as long as the CDC does not make such assistance a condition of the CDC accepting from that small business an application for a 504 loan. An example of other services a CDC

may provide is assisting a small business in applying for a 7(a) loan (as described in §120.2). A CDC is subject to part 103 of this chapter when providing such assistance.

[68 FR 57981, Oct. 7, 2003]

§ 120.828 Minimum level of 504 loan activity and restrictions on portfolio concentrations.

(a) A CDC is required to receive SBA approval of at least four 504 loan approvals during two consecutive fiscal years.

(b) A CDC's 504 loan portfolio must be diversified by business sector.

[68 FR 57981, Oct. 7, 2003]

§ 120.829 Job Opportunity average a CDC must maintain.

(a) A CDC's portfolio must maintain a minimum average of one Job Opportunity per an amount of 504 loan funding that will be specified by SBA from time to time in a FEDERAL REGISTER notice. Such Job Opportunity average remains in effect until changed by subsequent FEDERAL REGISTER publication. A CDC is permitted two years from its certification date to meet this average.

(b) A CDC must indicate in its annual report the Job Opportunities actually or estimated to be provided by each Project.

(c) If a CDC does not maintain the required average, it may retain its certification if it justifies to SBA's satisfaction its failure to do so in its annual report and shows how it intends to attain the required average.

[61 FR 3235, Jan. 31, 1996, as amended at 68 FR 57981, Oct. 7, 2003]

§ 120.830 Reports a CDC must submit.

A CDC must submit the following reports to SBA:

(a) An Annual Report within one hundred-eighty days after the end of the CDC's fiscal year (to include Federal tax returns for that year). A CDC that is certified by SBA within 6 months of the CDC's fiscal year-end is not required to submit an Annual Report for that year. The Annual Report must include, but is not limited to, the following:

(1) Audited or Reviewed Financial Statements as required in §120.826(c) and (d) for the CDC and any affiliates or subsidiaries of the CDC.

(i) Audited financial statements must, at a minimum, include the following:

(A) Audited balance sheet;

(B) Audited statement of income (or receipts) and expenses;

(C) Audited statement of source and application of funds;

(D) Such footnotes as are necessary to an understanding of the financial statements;

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

(F) The auditor's report; and

(ii) Reviewed financial statements must, at a minimum, include the following:

(A) Balance sheet;

(B) Statement of income (or receipts) and expenses;

(C) Statement of source and application of funds;

(D) Such footnotes as are necessary to an understanding of the financial statements;

(E) The accountant's review report; and

(2) Report on compensation: CDCs are required to provide detailed information on total compensation (including salary, bonuses and expenses) paid within the CDC's most recent tax year for current and former officers and directors, and for current and former employees and independent contractors with total compensation of more than $100,000 during that period.

(3) Certification of members of the Board of Directors. Written annual certification by each Board member that he or she has read and understands the requirements set forth in §120.823.

(4) Report on investment in economic development. Written report on investments in economic development in each State in which the CDC has an outstanding 504 loan.

(b) For each new associate and staff, a Statement of Personal History (for use by non-bank lenders and CDCs) and other information required by SBA;

(c) Reports of involvement in any legal proceeding;

(d) Changes in organizational status;

(e) Changes in any condition that affects its eligibility to continue to participate in the 504 program; and

(f) Quarterly service reports on each loan in its portfolio which is 60 days or more past due (and interim reports upon request by SBA).

(g) Other reports as required by SBA.

[61 FR 3235, Jan. 31, 1996, as amended at 68 FR 57981, Oct. 7, 2003; 73 FR 75518, Dec. 11, 2008; 79 FR 15650, Mar. 21, 2014]

EXTENDING A CDC'S AREA OF OPERATIONS

§ 120.835 Application to expand an Area of Operations.

(a) *General.* A CDC that has been certified to participate in the 504 program may apply to expand its Area of Operations if it meets all requirements to be an Accredited Lender Program (ALP) CDC, as set forth in §120.840(c), and demonstrates that it can competently fulfill its 504 program responsibilities in the proposed area.

(b) *Local Economic Area Expansion.* A CDC seeking to expand its Area of Operations into a Local Economic Area must apply in writing to the Lead SBA Office.

(c) A CDC seeking to become a Multi-State CDC must apply to the SBA District Office that services the area within each State where the CDC intends to locate its principal office for that State. A CDC may apply to be a Multi-State CDC only if the State the CDC seeks to expand into is contiguous to the State of the CDC's incorporation and the CDC establishes a loan committee in that State meeting the requirements of §120.823.

[68 FR 57981, Oct. 7, 2003, as amended at 79 FR 15650, Mar. 21, 2014]

EFFECTIVE DATE NOTE: At 84 FR 66295, Dec. 4, 2019, §120.835 was amended by adding a subject heading to paragraph (c), revising the last sentence of paragraph (c), and adding paragraphs (c)(1) and (2), effective Jan. 3, 2020. For the convenience of the user, the added and revised text is set forth as follows:

§ 120.835 January 3, 2020 Application to expand an Area of Operations.

* * * * *

(c) *Multi-State expansion.* * * * A CDC may apply to be a Multi-State CDC only if the State the CDC seeks to expand into is contiguous to the State of the CDC's incorporation and either:

(1) The CDC establishes a Loan Committee in the additional State consisting only of members who live or work in that State and that satisfies the other requirements in §120.823(d)(4)(ii)(A) through (D); or

(2) For any Project located in the additional State, the CDC's Board or Loan Committee (if established in the CDC's State of incorporation) includes at least two members who live or work in that State when voting on that Project. These two members may vote only on Projects located in the additional State.

§ 120.837 SBA decision on application for a new CDC or for an existing CDC to expand Area of Operations.

The processing District Office must solicit the comments of any other District Office in which the CDC operates or proposes to operate. The processing District Office must determine that the CDC is in compliance with SBA's regulations, policies, and performance benchmarks, including pre-approval and annual review by SBA of any management or staff contracts, and the timely submission of all annual reports. In making its recommendation on the application, the District Office may consider any information presented to it regarding the requesting CDC, the existing CDC, or CDCs that may be affected by the application, and the proposed Area of Operations.

(a) The SBA District office will submit the application, recommendation, and supporting materials within 60 days of the receipt of a complete application from the CDC to the D/FA, who will make the final decision. The D/FA may consider any information submitted or available related to the applicant and the application.

(b) SBA will notify the CDC of its decision in writing, and if the application is denied, the reasons for its decision.

(c) If a CDC is approved to operate as a Multi-State CDC, the CDC's ALP, PCLP, or Priority CDC authority will carry over into every additional State in which it is approved to operate as a Multi-State CDC.

[65 FR 42633, July 11, 2000, as amended at 68 FR 57981, Oct. 7, 2003]

§ 120.839 Case-by-case application to make a 504 loan outside of a CDC's Area of Operations.

A CDC may apply to make a 504 loan for a Project outside its Area of Operations by submitting a request to the 504 loan processing center. The applicant CDC must demonstrate that it can adequately fulfill its 504 program responsibilities for the 504 loan, including proper servicing. In addition, the CDC must have satisfactory SBA performance, as determined by SBA in its discretion. The CDC's Risk Rating, among other factors, will be considered in determining satisfactory SBA performance. Other factors may include, but are not limited to, review/examination assessments, historical performance measures, loan volume to the extent that it impacts performance measures, and other performance related measurements and information (such as contribution toward SBA mission). The 504 loan processing center may approve the application if:

(a) The applicant CDC has previously assisted the business to obtain a 504 loan; or

(b) The existing CDC or CDCs serving the area agree to permit the applicant CDC to make the 504 loan; or

(c) There is no CDC within the Area of Operations.

[68 FR 57982, Oct. 7, 2003, as amended at 73 FR 75518, Dec. 11, 2008; 82 FR 39504, Aug. 21, 2017]

EFFECTIVE DATE NOTE: At 84 FR 66296, Dec. 4, 2019, §120.839 was amended by adding the words ''or its affiliate(s)'' after ''business'' in paragraph (a), effective Jan. 3, 2020.

ACCREDITED LENDERS PROGRAM (ALP)

§ 120.840 Accredited Lenders Program (ALP).

(a) *General.* Under the ALP program, SBA designates qualified CDCs as ALP CDCs, gives them increased authority to process, close, and service 504 loans, and provides expedited processing of loan approval and servicing actions.

(b) *Application.* A CDC must apply for ALP status to the Lead SBA Office. The Lead SBA Office will send its recommendation and the application to the D/FA for final decision.

(c) *Eligibility.* In order for a CDC to be eligible to receive ALP status, its application must show that it meets the criteria set forth in §120.841.

(d) *Additional application requirements.* The CDC's application must include the following:

(1) Certified copy of the CDC's Board of Directors' resolution authorizing the application for ALP status.

(2) Summary of the experience of each of the CDC's loan processing, closing, and servicing staff members with significant authority.

(3) Name, address, and summary of experience of Designated Attorney.

(4) Documentation of any SBA required insurance.

(5) Any other documentation required by SBA.

(e) *Term of ALP designation.* SBA generally will designate a CDC as an ALP CDC for a two-year period. SBA may renew the designation for additional two-year periods if the CDC continues to meet the ALP program eligibility requirements.

(f) *SBA approval or decline decision.* SBA will notify the CDC in writing of an approval or decline of either an ALP application or of an ALP renewal. If the SBA approves the CDC's application, the ALP CDC may exercise its ALP authority in its entire Area of Operations. If an application or renewal is declined, SBA will notify the CDC of the reasons for the decision.

[68 FR 57982, Oct. 7, 2003]

§ 120.841 Qualifications for the ALP.

An applicant for ALP status must show that it substantially meets the following criteria:

(a) *CDC staff experience.* The CDC's staff must have well-trained, qualified loan officers who are knowledgeable concerning SBA's lending policies and procedures for the 504 program. The CDC must have at least one loan officer with three years of 504 loan processing experience and at least one loan officer with three years of 504 servicing experience or two years experience plus satisfactory completion of SBA-approved processing and servicing training. The same loan officer may meet these qualifications. In addition, the CDC's staff must have demonstrated satisfactorily to SBA the ability to process and service 504 loans.

(b) *Number of 504 loans approved and size of portfolio.* SBA must have approved at least 20 504 loan applications by the CDC in the most recent three years, and the CDC must have a portfolio of at least 30 active 504 loans. (An ''active'' 504 loan is a loan that was approved and closed by the CDC and has a status of either current, delinquent, or in liquidation.)

(c) *CDC reviews.* CDC reviews conducted by SBA must be current (within the last 24 months, if applicable) for applicants for ALP status. The CDC must have received a review assessment of either ''Acceptable'' or ''Acceptable With Corrective Actions Required.'' In addition, the CDC must have satisfactory SBA performance, as determined by SBA in its discretion. The CDC's Risk Rating, among other factors, will be considered in determining satisfactory SBA performance. Other factors may include, but are not limited to, review/examination assessments, historical performance measures, loan volume to the extent that it impacts performance measures, and other performance related measurements and information (such as contribution toward SBA mission);

(d) *Record of compliance with 504 program requirements.* The CDC must have a record of conforming to SBA's policies and procedures and of satisfactorily underwriting, closing and servicing 504 loans. SBA will consider all relevant material information, which will include but is not limited to whether the CDC meets all SBA's CDC portfolio benchmarks, when determining the CDC's record of compliance, including:

(1) Submission of satisfactory 504 loan analyses and applications, and all required, and properly completed, loan documents.

(2) Careful and thorough analysis and screening of all 504 loan applications for conformance with SBA credit and eligibility standards;

(3) Proper completion of required 504 loan closing documents and compliance with SBA 504 loan closing policies and procedures.

(4) Compliance with SBA loan servicing policies and procedures.

(5) Compliance with the certification and operational requirements as set forth in §§ 120.820 through 120.830.

(6) Submission of timely, complete and acceptable annual reports.

(7) Compliance with CDC ethical requirements (see § 120.851).

(e) *Priority CDC.* The CDC must be a Priority CDC with a Designated Attorney and SBA required insurance.

(f) *Record of Cooperation.* The CDC must have a record of effective communication and a cooperative relationship with all SBA offices including district offices and SBA's loan processing and servicing centers.

[68 FR 57982, Oct. 7, 2003, as amended at 72 FR 18364, Apr. 12, 2007; 73 FR 75519, Dec. 11, 2008; 82 FR 39504, Aug. 21, 2017]

PREMIER CERTIFIED LENDERS PROGRAM

§ 120.845 Premier Certified Lenders Program (PCLP).

(a) *General.* Under the PCLP, SBA designates qualified CDCs as PCLP CDCs and delegates to them increased authority to process, close, service, and liquidate 504 loans. SBA also may give PCLP CDCs increased authority to litigate 504 loans.

(b) *Application.* A CDC must apply for PCLP status to the Lead SBA Office. The Lead SBA Office will send its written recommendation and the application to SBA's PCLP Loan Processing Center. The PCLP Loan Processing Center will review these materials and forward them to the appropriate Office of Capital Access official in accordance with Delegations of Authority for final determination.

(c) *Eligibility.* In order for a CDC to be eligible to receive PCLP status, its application must show that it meets the following criteria:

(1) The CDC must be an ALP CDC in substantial compliance with Loan Program Requirements or meet the criteria to be an ALP CDC set forth in § 120.841(a) through (h).

(2) The CDC can adequately comply with SBA liquidation and litigation requirements.

(d) *Additional application requirements.* The application must include the following:

(1) Certified copy of the CDC's Board of Directors' resolution authorizing the application for PCLP status.

(2) Summary of the experience of each of the CDC's loan processing, closing, servicing and liquidation staff members with significant authority.

(3) Name, address and summary of experience of Designated Attorney.

(4) Documentation of any SBA required insurance.

(5) Any other documentation required by SBA.

(e) *Term of designation.* If approved, SBA generally will confer PCLP status for a period of two years. However, if SBA deems it appropriate, it may confer PCLP status for a period of less than two years.

(f) *Area of Operations for PCLP CDCs.* If the SBA approves the CDC's application, the PCLP CDC may exercise its PCLP authority in its entire Area of Operations.

(g) *SBA approval or decline decision.* SBA will notify the CDC in writing of an approval or decline of a PCLP application. If an application is declined, SBA will notify the CDC of the reasons for the decision.

[68 FR 57982, Oct. 7, 2003, as amended at 72 FR 18364, Apr. 12, 2007; 73 FR 75519, Dec. 11, 2008]

§ 120.846 Requirements for maintaining and renewing PCLP status.

(a) To maintain its status as a PCLP CDC, a CDC must continue to:

(1) Meet the PCLP eligibility requirements in § 120.845.

(2) Timely conform with all requirements and deadlines set forth in SBA's regulations and policy and procedural guidance concerning properly establishing, funding and reporting a PCLP Loan Loss Reserve Fund (LLRF).

(3) Substantially comply with all Loan Program Requirements.

(4) Remain an active CDC.

(5) In accordance with statutory requirements set forth in section 508(i) of Title V, 15 U.S.C. 697e(i), establish a goal of processing at least 50 percent of its 504 loans using PCLP procedures.

(b) SBA will notify the PCLP CDC in writing of a renewal or non-renewal of PCLP status. If PCLP status is not renewed, SBA will notify the CDC of the reasons for the decision.

[68 FR 57983, Oct. 7, 2003, as amended at 72 FR 18364, Apr. 12, 2007]

§ 120.847 Requirements for the Loan Loss Reserve Fund (LLRF).

(a) *General.* PCLP CDCs must establish and maintain a LLRF (or multiple accounts which together constitute one LLRF) which complies with paragraphs (b) through (g) of this section. A PCLP CDC must use the LLRF or other funds to reimburse the SBA for 10 percent of any loss sustained by SBA as a result of a default in the payment of principal or interest on a Debenture it issued under the PCLP (''PCLP Debenture''). A CDC that is participating in the PCLP as of January 1, 2004, and a CDC that has participated in the PCLP in the past but which does not have PCLP status as of that date, must establish a LLRF within 30 days of that date to cover potential losses for all 504 loans made in connection with PCLP Debentures that remain outstanding as of that date. A CDC that receives PCLP status after that date must establish and maintain a LLRF prior to closing any 504 loans processed under its PCLP status. The LLRF is the accumulation of deposits that a PCLP CDC must establish and maintain for each PCLP Debenture that it issues. PCLP CDCs must coordinate with their Lead SBA Office to ensure that the LLRF is properly established, that all necessary documentation is executed and delivered by all parties in a timely fashion, and that all required deposits are made.

(b) *PCLP CDC Exposure and LLRF deposit requirements.* A PCLP CDC's ''Exposure'' is defined as its reimbursement obligation to SBA with respect to default in the payment of any PCLP Debenture. The amount of a PCLP CDC's Exposure is 10 percent of any loss (including attorney's fees; litigation costs; and care of collateral, appraisal and other liquidation costs and expenses) sustained by SBA as a result of a default in the payment of principal or interest on a PCLP Debenture. For each PCLP Debenture a PCLP CDC issues, it must establish and maintain an LLRF equal to one percent of the original principal amount (the face

amount) of the PCLP Debenture. The amount the PCLP CDC must maintain in the LLRF for each PCLP Debenture remains the same even as the principal balance of the PCLP Debenture is paid down over time.

(c) *Establishing a LLRF.* The LLRF must be a deposit account (or accounts) with a federally insured depository institution selected by the PCLP CDC. A ''deposit account'' is a demand, time, savings, or passbook account, including a certificate of deposit (CD) which is either uncertificated or, if certificated, non-transferable. A ''deposit account'' is not an investment account and must not contain securities or other investment properties. A deposit account may contain only cash and CDs credited to that account. A PCLP CDC may pool its deposits for multiple PCLP Debentures in a single account in one institution. The LLRF must be segregated from the PCLP CDC's other operating accounts. The PCLP CDC is responsible for all fees, costs and expenses incurred in connection with establishing, managing and maintaining the LLRF, including fees associated with transferring funds or early withdrawal of CDs, and related income tax expenses.

(d) *Creating and perfecting a security interest in a LLRF.* A PCLP CDC must give SBA a first priority, perfected security interest in the LLRF to secure the PCLP CDC's obligation to reimburse SBA for the PCLP CDC's Exposure under all of its outstanding PCLP Debentures. (If a PCLP CDC's LLRF is comprised of multiple deposit accounts, it must give SBA this security interest with respect to each such account.) The PCLP CDC must grant to SBA the security interest in the LLRF pursuant to a security agreement between the PCLP CDC and SBA, and a control agreement between the PCLP CDC, SBA, and the applicable depository institution. The control agreement must include provisions requiring the depository institution to follow SBA instructions regarding withdrawal from the account without a requirement for obtaining further consent from the PCLP CDC, and must restrict the PCLP CDC's ability to make withdrawals from the account without SBA consent. When establishing the LLRF, a PCLP CDC must coordinate with its Lead SBA Office to execute and deliver the required documentation. The PCLP CDC must provide to the Lead SBA Office a fully executed original of the security and control agreements. All documents must be satisfactory to SBA in both form and substance.

(e) *Schedule for contributions to a LLRF.* The PCLP CDC must contribute to the LLRF the required deposits for each PCLP Debenture in accordance with the following schedule:

(1) At least 50 percent of the required deposits to the LLRF on or about the date that it issues the PCLP Debenture.

(2) At least an additional 25 percent of the required deposits to the LLRF no later than one year after it issues the PCLP Debenture.

(3) Any remainder of the required deposits to the LLRF no later than two years after it issues the PCLP Debenture.

(f) *LLRF reporting requirements.* Each PCLP CDC must periodically report to SBA the amount in the LLRF in a form that will readily facilitate reconciliation of the amount maintained in the LLRF with the amount required to meet a PCLP CDC's Exposure for its entire portfolio of PCLP Debentures.

(g) *Withdrawal of excess funds.* Interest and other funds in the LLRF that exceed the required minimums as set forth in paragraph (b) of this section, within the time frames set forth in paragraph (e) of this section, accrue to the benefit of the PCLP CDC. PCLP CDCs are authorized to withdraw excess funds, including interest, from the LLRF if such funds exceed the required minimums set forth in paragraph (b) of this section. The PCLP CDC must forward requests for withdrawals to the Lead SBA Office, which will verify the existence and amount of excess funds and notify the financial institution to transfer the excess funds to the PCLP CDC.

(h) *Determining SBA loss.* When a PCLP CDC has concluded the liquidation of a defaulted 504 loan made with the proceeds of a PCLP Debenture and has submitted a liquidation wrap-up report to SBA, or when SBA otherwise

determines that the PCLP CDC has exhausted all reasonable collection efforts with respect to that 504 loan, SBA will determine the amount of the loss to SBA. SBA will notify the PCLP CDC of the amount of its reimbursement obligation to SBA (if any) and will explain how SBA calculated the loss.

(1) If the PCLP CDC agrees with SBA's calculations of the loss, it must reimburse SBA for ten percent of the amount of that loss no later than 30 days after SBA's notification to the PCLP CDC of the CDC's reimbursement obligation.

(2) If the PCLP CDC disputes SBA's calculations, it must reimburse SBA for ten percent of any loss amount that is not in dispute no later than 30 days after SBA's notification to the PCLP CDC of the CDC's reimbursement obligation. No later than 30 days after SBA's notification, the PCLP CDC may submit to the D/FA or his or her delegate a written appeal of any disagreement regarding the calculation of SBA's loss. The PCLP CDC must include with that appeal an explanation of its reasons for the disagreement. Upon the D/FA's final decision as to the disputed amount of the loss, the PCLP CDC must promptly reimburse SBA for ten percent of that amount.

(i) *Reimbursing SBA for loss.* A PCLP CDC may use funds in the LLRF or other funds to reimburse SBA for the PCLP CDC's Exposure on a defaulted PCLP Debenture. If a PCLP CDC does not satisfy the entire reimbursement obligation within 30 days after SBA's notification to the PCLP CDC's of its reimbursement obligation, SBA may cause funds in the LLRF to be transferred to SBA in order to cover the PCLP CDC's Exposure, unless the PCLP CDC has filed an appeal under paragraph (h)(2) of this section. If the PCLP CDC has filed such an appeal, SBA may cause such a transfer of funds to SBA 30 days after the D/FA's or his or her delegate's decision. If the LLRF does not contain sufficient funds to reimburse SBA for any unpaid Exposure with respect to any PCLP Debenture, the PCLP CDC must pay SBA the difference within 30 days after demand for payment by SBA.

(j) *Insufficient funding of LLRF.* A PCLP CDC must diligently monitor the LLRF to ensure that it contains sufficient funds to cover its Exposure for its entire portfolio of PCLP Debentures. If, at any time, the LLRF does not contain sufficient funds, the PCLP CDC must, within 30 days of the earlier of the date it becomes aware of this deficiency or the date it receives notification from SBA of this deficiency, make additional contributions to the LLRF to make up this difference.

[68 FR 57983, Oct. 7, 2003]

EFFECTIVE DATE NOTE: At 84 FR 66296, Dec. 4, 2019, §120.847 was amended by revising the third and fourth sentences in paragraph (b) and adding paragraphs (b)(1) and (2), effective Jan. 3, 2020. For the convenience of the user, the added and revised text is set forth as follows:

§ 120.847 Requirements for the Loan Loss Reserve Fund (LLRF).

* * * * *

(b) * * * For each PCLP Debenture a PCLP CDC issues, it must establish and maintain an LLRF equal to one percent of the original principal amount of the PCLP Debenture. The amount the PCLP CDC must maintain in the LLRF for each PCLP Debenture remains the same even as the principal balance of the PCLP Debenture is paid down over time except that, after the first 10 years of the term of the Debenture, the amount maintained in the LLRF may be based on one percent of the current principal amount of the PCLP Debenture (the declining balance methodology), as determined by SBA. All withdrawals must be made in accordance with the requirements of paragraph (g) of this section. A CDC may not use the declining balance methodology:

(1) With respect to any Debenture that has been purchased. Within 30 days after purchase, the CDC must restore the balance maintained in the LLRF for the Debenture that was purchased to one percent of the original principal amount of that Debenture; or

(2) With respect to any other Debenture if SBA notifies the CDC in writing that it has failed to satisfy the requirements in paragraph (e), (f), (h), (i), or (j) of this section. In such case, the CDC will not be required to restore the balance maintained in the LLRF to one percent of the original principal amount of the Debenture but must base the amount maintained in the LLRF on one percent of the principal amount of the Debenture as of the date of notification. The CDC may not begin to use the declining balance methodology again until SBA notifies the CDC in

writing that SBA has determined, in its discretion, that the CDC has corrected the noncompliance and has demonstrated its ability to comply with these requirements.

* * * * *

§ 120.848 Requirements for 504 loan processing, closing, servicing, liquidating, and litigating by PCLP CDCs.

(a) *General.* In processing closing, servicing, liquidating and litigating 504 loans under the PCLP (''PCLP Loans''), the PCLP CDC must comply with Loan Program Requirements and conduct such activities in accordance with prudent and commercially reasonable lending standards.

(b) *Documentation of decision making.* For each PCLP Loan, the PCLP CDC must document in its files the basis for its decisions with respect to loan processing, closing, servicing, liquidating, and litigating.

(c) *Processing requirements.* SBA expects PCLP CDCs to handle most 504 loan processing situations, although SBA may require that the PCLP CDC process 504 loans involving complex or problematic eligibility issues through the SBA using standard 504 loan processing procedures. The PCLP CDC is responsible for properly determining borrower creditworthiness and establishing the terms and conditions under which the PCLP Loan will be made. The PCLP CDC also is responsible for properly undertaking such other processing actions as SBA may delegate to the PCLP CDC.

(d) *Submission of loan documents.* A PCLP CDC must notify SBA of its approval of a 504 loan by submitting to SBA's PCLP Loan Processing Center all documentation required by SBA, including SBA's PCLP eligibility checklist, signed by an authorized representative of the PCLP CDC. The PCLP Loan Processing Center will review these documents to determine whether the PCLP CDC has identified any problems with the PCLP Loan approval, and whether SBA funds are available for the PCLP Loan. If appropriate, the PCLP Processing Center will notify the PCLP CDC of the loan number assigned to the loan.

(e) *Loan and Debenture closing.* After receiving notification from SBA PCLP Loan Processing Center, the PCLP CDC is responsible for properly undertaking all actions necessary to close the PCLP Loan and Debenture in accordance with the expedited loan closing procedures applicable to a Priority CDC and with § 120.960.

(f) *Servicing, liquidation and litigation responsibilities.* The PCLP CDC generally must service, liquidate and litigate its entire portfolio of PCLP Loans, although SBA may in certain circumstances elect to handle such duties with respect to a particular PCLP Loan or Loans. Additional servicing and liquidation requirements are set forth in subpart E of this part.

(g) *Making a 504 loan previously considered by another CDC.* A PCLP CDC also may utilize its PCLP status to process a 504 loan application from an applicant whose application was declined or rejected by another CDC operating in that same Area of Operations, if the applicant is located within that area and as long as SBA has not previously declined that applicant's 504 loan application. This may include the processing of a 504 loan application from an applicant that has withdrawn its application from another CDC.

[68 FR 57984, Oct. 7, 2003, as amended at 72 FR 18364, Apr. 12, 2007]

ASSOCIATE DEVELOPMENT COMPANIES (ADCS)

§ 120.850 Expiration of Associate Development Company designation.

The designation of Associate Development Company (ADC) will cease to exist on January 1, 2004. After that date, former ADCs may continue to contract with CDCs as Lender Service Providers (see part 103 of this chapter) or to perform other services.

[68 FR 57984, Oct. 7, 2003]

OTHER CDC REQUIREMENTS

§ 120.851 CDC ethical requirements.

CDCs and their Associates must act ethically and exhibit good character. They must meet all of the ethical requirements of § 120.140. In addition, they are subject to the following:

(a) Any benefit flowing to a CDC's Associate or his or her employer from activities as an Associate must be

merely incidental (this requirement does not prevent an Associate or an Associate's employer from providing interim financing as described in § 120.890 or Third Party Loans as described in § 120.920, as long as such activity does not violate § 120.140); and

(b) A CDC's Associate may not be an officer, director, or manager of more than one CDC.

[68 FR 57984, Oct. 7, 2003]

§ 120.852 [Reserved]

§ 120.853 Inspector General audits of CDCs.

The SBA Office of Inspector General may also conduct, supervise or coordinate audits pursuant to the Inspector General Act. The CDC must cooperate and make its staff, records, and facilities available.

[68 FR 57985, Oct. 7, 2003, as amended at 73 FR 75519, Dec. 11, 2008]

§ 120.857 Voluntary transfer and surrender of CDC certification.

A CDC may not transfer its certification or withdraw from the 504 program without SBA's consent. The CDC must provide a plan to SBA to transfer its portfolio. The portfolio may only be transferred with SBA's written consent. If a CDC desires to withdraw from the 504 program, it must forfeit its portfolio to SBA. SBA may conduct an audit of the transferring or withdrawing CDC.

[61 FR 3235, Jan. 31, 1996. Redesignated at 68 FR 57987, Oct. 7, 2003]

PROJECT ECONOMIC DEVELOPMENT GOALS

§ 120.860 Required objectives.

A Project must achieve at least one of the economic development objectives set forth in § 120.861 or § 120.862.

§ 120.861 Job creation or retention.

A Project must create or retain one Job Opportunity per an amount of 504 loan funding that will be specified by SBA from time to time in a FEDERAL REGISTER notice. Such Job Opportunity average remains in effect until changed by subsequent FEDERAL REGISTER publication.

[68 FR 57987, Oct. 7, 2003]

§ 120.862 Other economic development objectives.

A Project that achieves any of the following community development or public policy goals is eligible if the CDC's overall portfolio of 504 loans, including the subject loan, meets or exceeds the CDC's required Job Opportunity average. Loan applications must indicate how the Project will meet the specified economic development objective.

(a) Community Development goals:

(1) Improving, diversifying or stabilizing the economy of the locality;

(2) Stimulating other business development;

(3) Bringing new income into the community;

(4) Assisting manufacturing firms (North American Industry Classification System (NAICS), Sectors 31 '' 33); or

(5) Assisting businesses in Labor Surplus Areas as defined by the Department of Labor.

(b) Public Policy goals:

(1) Revitalizing a business district of a community with a written revitalization or redevelopment plan;

(2) Expansion of exports;

(3) Expansion of small businesses owned and controlled by women as defined in section 29(a)(3) of the Act, 15 U.S.C. 656(a)(3);

(4) Expansion of small businesses owned and controlled by veterans (especially service-disabled veterans) as defined in section 3(q) of the Act, 15 U.S.C. 632(q);

(5) Expansion of minority enterprise development (see § 124.103(b) of this chapter for minority groups who qualify for this description);

(6) Aiding rural development;

(7) Increasing productivity and competitiveness (retooling, robotics, modernization, competition with imports);

(8) Modernizing or upgrading facilities to meet health, safety, and environmental requirements;

(9) Assisting businesses in or moving to areas affected by Federal budget reductions, including base closings, either because of the loss of Federal contracts or the reduction in revenues in the area due to a decreased Federal presence; or

(10) Reduction of rates of unemployment in labor surplus areas, as such areas are determined by the Secretary of Labor.

[61 FR 3235, Jan. 31, 1996, as amended at 64 FR 2118, Jan. 13, 1999; 68 FR 57987, Oct. 7, 2003; 76 FR 63547, Oct. 12, 2011]

LEASING POLICIES SPECIFIC TO 504 LOANS

§ 120.870 Leasing Project Property.

(a) A Borrower may use the proceeds of a 504 loan to acquire, construct, or modify buildings and improvements, and/or to purchase and install machinery and equipment located on land leased to the Borrower by an unrelated lessor if:

(1) The remaining term of the lease, including options to renew, exercisable only by the lessee, equals or exceeds the term of the Debenture;

(2) The Borrower assigns its interest in the lease to the CDC with right of reassignment to SBA; and

(3) The 504 loan is secured by a recorded lien against the leasehold estate and other collateral as necessary.

(b) If the Project is for new construction, the Borrower may lease long term up to 20 percent of the Rentable Property in the Project to one or more tenants if the Borrower immediately occupies at least 60 percent of the Rentable Property, plans to occupy within three years some of the remaining space not immediately occupied and not leased long term, and plans to occupy all of the remaining space not leased long term within ten years.

[61 FR 3235, Jan. 31, 1996, as amended at 64 FR 2118, Jan. 13, 1999; 68 FR 57987, Oct. 7, 2003]

§ 120.871 Leasing part of Project Property to another business.

(a) The costs of interior finishing of space to be leased out to another business are not eligible Project costs.

(b) Third-party loan proceeds used to renovate the leased space do not count towards the 504 first mortgage requirement or the Borrower's contribution.

LOAN-MAKING POLICIES SPECIFIC TO 504 LOANS

§ 120.880 Basic eligibility requirements.

In addition to the eligibility requirements specified in subpart A, to be an eligible Borrower for a 504 loan, a small business must:

(a) Use the Project Property (except that an Eligible Passive Company may lease to an Operating Company); and

(b) Together with its Affiliates, meet one of the size standards set forth in §121.301(b) of this chapter.

[61 FR 3235, Jan. 31, 1996, as amended at 68 FR 57987, Oct. 7, 2003]

§ 120.881 Ineligible Projects for 504 loans.

In addition to the ineligible businesses and uses of proceeds specified in subpart A of this part, the following Projects are ineligible for 504 financing:

(a) Relocation of any of the operations of a small business which will cause a net reduction of one-third or more in the workforce of a relocating small business or a substantial increase in unemployment in any area of the country, unless the CDC can justify the loan because:

(1) The relocation is for key economic reasons and crucial to the continued existence, economic wellbeing, and/or competitiveness of the applicant; and

(2) The economic development benefits to the applicant and the receiving community outweigh the negative impact on the community from which the applicant is moving; and

(b) Projects in foreign countries (loans financing real or personal property located outside the United States or its possessions).

§ 120.882 Eligible Project costs for 504 loans.

Eligible Project costs which may be paid with the proceeds of 504 loans are:

(a) Costs directly attributable to the Project including expenditures incurred by the Borrower (with its own funds or from a loan) to acquire land

used in the Project, or for any other expense directly attributable to the Project, prior to applying to SBA for the 504 loan;

(b) In Projects involving construction, a contingency reserve for cost overruns not to exceed 10 percent of construction cost;

(c) Professional fees directly attributable and essential to the Project, such as title insurance, opinion of title, architectural and engineering costs, appraisals, environmental studies, and legal fees related to zoning, permits, or platting; and

(d) Repayment of interim financing including points, fees and interest.

(e) If the project involves expansion of a small business concern, any amount of existing indebtedness that does not exceed 50 percent of the project cost of the expansion may be refinanced and added to the expansion cost if:

(1) Substantially all (85% or more) of the proceeds of the indebtedness were used to acquire land, including a building situated thereon, to construct a building thereon, or to purchase equipment. The assets acquired must be eligible for financing under the 504 loan program. If the acquisition, construction or purchase of the asset was originally financed through a commercial loan that would have satisfied the ''substantially all'' requirement and that was subsequently refinanced one or more times, with the current commercial loan being the most recent refinancing, the current commercial loan will be deemed to satisfy this paragraph (e)(1).

(2) The existing indebtedness is collateralized by fixed assets. The 504 eligible fixed assets collateralizing any debt to be refinanced or relating to the portion of debt being refinanced in the case of a partial refinance must also collateralize the 504 Loan unless SBA approves a waiver due to extraordinary circumstances. PCLP CDCs may not use their delegated authority to approve a loan requiring this waiver;

(3) The existing indebtedness was incurred for the benefit of the small business concern for which any new Project costs are incurred. Existing 7(a) and 504 loans may be refinanced under this section in accordance with SBA policies or procedures;

(4) The financing will be used only for refinancing existing indebtedness or costs relating to the project financed;

(5) The financing will provide a substantial benefit to the borrower when prepayment penalties, financing fees, and other financing costs are accounted for. For purposes of this paragraph, ''substantial benefit'' means that the portion of the new installment amount attributable to the debt being refinanced must be at least 10 percent less than the existing installment amount(s). Prepayment penalties, financing fees, and other financing costs must also be added to the amount being refinanced in calculating the percentage reduction in the new installment payment. Exceptions to the 10% reduction requirement may be approved by the D/FA or designee for good cause. PCLP CDCs may not use their delegated authority to approve a loan requiring this exception;

(6) The borrower has been current on all payments due on the existing debt for not less than 1 year preceding the date of refinancing. For purposes of this section, ''date of refinancing'' refers to the date the 504 loan is approved by SBA. Any unremedied delinquency after approval must be reported to SBA as an adverse change;

(7) The financing under section 504 will provide better terms or rate of interest than the existing indebtedness on the date of refinancing. For purposes of this paragraph, ''better terms or rate of interest'' may include longer maturity (but always commensurate with the assets' useful life), a lower interest rate committed on the Third Party Lender Loan or projected on the 504 loan, improved collateral conditions, or less restrictive loan covenants.

(8) The authority to approve the refinancing of same institution debt must be approved by SBA and is not delegated to the PCLP CDCs. For the purposes of this paragraph, ''same institution debt'' means any debt of the CDC or the Third Party Lender financing the new project, or of affiliates of either.

(f) For the purposes of paragraph (e), the phrase ''project involves expansion

of a small business concern'' includes any project that involves the acquisition, construction or improvement of land, building or equipment for use by the small business concern.

(g) SBA may approve a Refinancing Project of a qualified debt subject to the following conditions and requirements:

(1) The Refinancing Project does not involve the expansion of a small business;

(2) The applicant for the refinancing available under this paragraph (g) has been in operation for all of the 2 year period ending on the date of application;

(3) The cost to the Federal Government of making guarantees under this subsection (g) and under section 503 of the Small Business Investment Act of 1958 (15 U.S.C. 697) during the fiscal year in which the guarantee is made is zero;

(4) In addition to the annual guarantee fee assessed under §120.971(d)(2), Borrower must pay SBA a supplemental annual guarantee fee to cover the additional cost attributable to the refinancing in an amount established by SBA each fiscal year.

(5) The funding for the Refinancing Project must come from three sources based on the current fair market value of the fixed assets serving as collateral for the Refinancing Project, including a Third Party Loan that is at least as much as the 504 loan, not less than 10% from the Borrower (excluding administrative costs), and not more than 40% from the 504 loan. If the Refinancing Project involves a limited or single purpose building or structure, the Borrower must contribute not less than 15% (excluding administrative costs), unless SBA determines, in its discretion, and publishes a notice in the FEDERAL REGISTER, that due to an economic recession, as determined by the National Bureau of Economic Research or its equivalent, Borrowers may contribute not less than 10% for Refinancing Projects involving a limited or single purpose property during the recession. The lower required contribution by the Borrower will be in effect until the first day of the calendar quarter following the end of the economic recession as determined by the National Bureau of Economic Research or its equivalent. SBA will publish a notice in the FEDERAL REGISTER announcing the date on which the requirement of the lower Borrower contribution ended. In addition to a cash contribution, the Borrower's contribution may be satisfied as set forth in §120.910 or by the equity in any other fixed assets that are acceptable to SBA as collateral for the Refinancing Project, provided that there is an independent appraisal of the fair market value of the asset;

(6)(i) The portion of the Refinancing Project provided by the 504 loan and the Third Party Loan may be no more than 90% of the fair market value of the fixed assets that will serve as collateral, except that if the Borrower's application includes a request to finance the Eligible Business Expenses described in paragraph (g)(6)(ii) of this section, the portion of the Refinancing Project provided by the 504 loan and the Third Party Loan may be no more than 85% of the fair market value of the fixed assets that will serve as collateral and the Borrower may receive no more than 20% of the fair market value of the Eligible Fixed Asset(s) securing the Qualified Debt for Eligible Business Expenses;

(ii) The Borrower's application may include a request to finance eligible business expenses as part of the Refinancing Project if the amount of cash funds that will be provided for the Refinancing Project exceeds the amount to be paid to the lender of the Qualified Debt. The Borrower's application must include a specific description of the business expenses for which the financing is requested and an itemization of the amount of each expense. For the purposes of this paragraph (g), ''Eligible Business Expenses'' are limited to the operating expenses of the business that were incurred but not paid prior to the date of application or that will become due for payment within 18 months after the date of application. These expenses may include salaries, rent, utilities, inventory, and other expenses of the business that are not capital expenditures. Debt is not included as an Eligible Business Expense, except debt that was incurred with a credit card or a business line of credit may be

included if the credit card or business line of credit is issued in the name of the small business and the Applicant certifies that the debt being refinanced was incurred exclusively for business related purposes. Loan proceeds must not be used to refinance any personal expenses. Both the CDC and the Borrower must certify in the application that the funds will be used to cover Eligible Business Expenses. Borrower must, upon request, substantiate the use of the funds provided for business expenses through, for example, bank statements, invoices marked ''paid,'' cleared checks, or any other documents that demonstrate that a business obligation was satisfied with the funds provided.

(7) If the qualified debt is not fully satisfied by the funding provided by the Refinancing Project, the lender of the qualified debt must take one of the following actions, or some combination thereof, to address the deficiency:

(i) Forgiveness of all or part of the deficiency;

(ii) Acceptance of payment by the Borrower, or

(iii) Acceptance of a Note executed by the Borrower for the balance, or any portion of the balance. Such Note must be subordinate to the 504 loan if the Note and the 504 loan are secured by any of the same collateral. The Note is subject to any other restrictions that SBA may establish to protect its creditor position, including standby requirements;

(8) The Third Party Lender must have a first lien position, and the 504 loan must have a second lien position, on all Eligible Fixed Assets securing the Refinancing Project. Any other lien must be junior in priority to these lien positions. For other fixed assets serving as collateral for the Refinancing Project, the lien positions of the Third Party Lender and the 504 loan may be junior to any existing liens acceptable to SBA;

(9) Eligible Project costs which may be paid with the proceeds of the 504 loan are the amount used to refinance the qualified debt and other costs under §120.882(c) and (d) and eligible administrative costs under §120.883;

(10) A CDC must limit the amount of its loans under this paragraph (g) so that, during any Federal fiscal year, the amount of the new loans approved under this paragraph (g) does not exceed 50% of the total dollar amount of the CDC's 504 loans approved (including the loans approved under this paragraph (g)) during the previous fiscal year. This limitation may be waived upon application by the CDC and upon a determination by SBA that the 504 loan is needed for good cause.

(11) The authority to approve the refinancing under this paragraph (g) is not delegated to PCLP CDCs;

(12) The 504 loans approved under this paragraph (g) must be disbursed within 9 months after loan approval. The Director, Office of Financial Assistance, or his or her designee, may approve a request for extension of the disbursement period for an additional 6 months for good cause.

(13) The Third Party Loan may not be sold on the secondary market as a part of a pool guaranteed under subpart J of this part, or any successor to this program, when the debt being refinanced is same institution debt;

(14) The Third Party Lender must certify that it would not refinance the qualified debt except for the assistance provided under this paragraph (g);

(15) *Definitions.* For the purposes of this paragraph (g), the terms below are defined as follows:

Date of application refers to the date the 504 loan application is received by SBA.

Eligible Fixed Assets are one or more long-term fixed assets, such as land, buildings, machinery, and equipment, acquired, constructed or improved by a small business for use in its business operations.

Fair market value refers to the current appraised value of an asset that is established by an independent appraiser in accordance with the standards established by SBA in its SOPs.

Qualified debt is a commercial loan:

(i) That was incurred not less than 2 years before the date of the application for the refinancing available under this paragraph (g). A commercial loan that was refinanced within the two years prior to the date of application (the most recent loan) may be deemed incurred not less than 2 years before the date of the application provided that

the effect of the most recent loan was to extend the maturity date without advancing any additional proceeds (except to cover closing costs) and the collateral for the most recent loan includes, at a minimum, the same Eligible Fixed Asset(s) that served as collateral for the former loan that was refinanced. The loan documents and lien instruments for the most recent loan, as well as the loan documents and lien instruments for the loan that was replaced by the most recent loan, must be submitted to SBA as part of the application.

(ii) That is not subject to a guarantee by a Federal agency or department;

(iii) Substantially all (85% or more) of which was for an Eligible Fixed Asset. If the Eligible Fixed Asset was originally financed through a commercial loan that would have satisfied the ''substantially all'' standard (the ''original loan'') and that was subsequently refinanced one or more times, with the current commercial loan being the most recent refinancing, the current commercial loan will be deemed to satisfy this paragraph (iii). If the original loan was for the construction of a new building, or the acquisition, renovation, or reconstruction of an existing building, and such loan would not have satisfied the leasing policies set forth in 13 CFR 120.131 and 13 CFR 120.870(b), the current commercial loan will be deemed to satisfy these policies, provided that Borrower demonstrates compliance with 13 CFR 120.131(b) for existing buildings as of the date of application.

(iv) That was for the benefit of the small business concern;

(v) That is collateralized by Eligible Fixed Assets;

(vi) That is not a Third Party Loan that is part of an existing 504 Project; and

(vii) For which the applicant for the refinancing available under this paragraph (g) has been current on all payments due for not less than one year preceding the date of application. For the purposes of this paragraph (vii), ''current on all payments due'' means that no payment was more than 30 days past due from either the original payment terms or modified payment terms (whether through a modification to an existing Note or through a refinancing that results in a new Note). The modification (or refinancing) must have been agreed to in writing by the Borrower and the lender of the existing debt no less than one year preceding the date of application, except that a modified (or refinanced) loan may be allowed if the purpose of the modification (or refinancing) was to extend the maturity date of the loan, including any balloon payment, and if, during the one year period prior to the date of application (*i.e.*, in the months prior to and after the modification or refinancing), the Borrower was current on all payments due, there have been no deferments of any payments, and no additional proceeds were advanced through the modification or refinancing (except to cover closing costs). Any delinquency in payment on the loan to be refinanced after approval and before debenture funding must be reported to SBA as an adverse change.

Refinancing Project means the fair market value of the Eligible Fixed Asset(s) securing the qualified debt and any other fixed assets acceptable to SBA, except that if the Refinancing Project includes the financing of Eligible Business Expenses, SBA will not accept as collateral any fixed assets other than the Eligible Fixed Asset(s) securing the Qualified Debt.

Same institution debt means any debt of the Third Party Lender that is providing funds for the refinancing, or of its affiliates.

[61 FR 3235, Jan. 31, 1996, as amended at 68 FR 57987, Oct. 7, 2003; 74 FR 29591, June 23, 2009; 76 FR 9218, Feb. 17, 2011; 76 FR 63155, Oct. 12, 2011; 79 FR 15650, Mar. 21, 2014; 81 FR 33125, May 25, 2016; 83 FR 19920, May 7, 2018]

§ 120.883 Eligible administrative costs for 504 loans.

The following administrative costs are not part of Project costs, but may be paid with the proceeds of the 504 loan and the Debenture (see § 120.971):

(a) SBA guarantee fee;

(b) Funding fee (to cover the cost of a public issuance of securities and the Trustee);

(c) CDC processing fee;

(d) Borrower's out-of-pocket costs associated with 504 loan and Debenture

closing other than legal fees (for example, certifications and the copying costs associated with them, overnight delivery, postage, and messenger services) but not to include fees and costs described in § 120.882;

(e) CDC Closing Fee (see § 120.971(a)(2)) up to a maximum of $2,500; and

(f) Underwriters' fee.

[64 FR 2118, Jan. 13, 1999, as amended at 68 FR 57987, Oct. 7, 2003]

§ 120.884 Ineligible costs for 504 loans.

Costs not directly attributable and necessary for the Project may not be paid with proceeds of the 504 loan. These include, but are not limited to, the following:

(a) Debt refinancing (other than interim financing), except as provided in § 120.882(e) and (g).

(b) A CDC may not use 504 loan proceeds to pay any creditor in a position to sustain a loss causing a shift to SBA of all or part of a potential loss from an existing debt.

(c) Third-Party Loan fees (commitment, broker, finders, origination, processing fees of permanent financing).

(d) Ancillary business expenses, such as:

(1) Working capital;

(2) Counseling or management services fees;

(3) Incorporation/organization costs;

(4) Franchise fees; and

(5) Advertising.

(e) Fixed-asset Project components, such as:

(1) Short-term equipment, furniture, and furnishings (unless essential to and a minor portion of the Project);

(2) Automobiles, trucks, and airplanes; and

(3) Construction equipment (except for heavy duty construction equipment integral to the business' operations with a remaining useful life of a minimum of 10 years).

[61 FR 3235, Jan. 31, 1996, as amended at 64 FR 2118, Jan. 13, 1999; 74 FR 29591, June 23, 2009; 76 FR 9219, Feb. 17, 2011; 82 FR 39504, Aug. 21, 2017]

INTERIM FINANCING

§ 120.890 Source of interim financing.

A Project may use interim financing for all Project costs except the Borrower's contribution. Any source (including a CDC) may supply interim financing provided:

(a) The financing is not derived from any SBA program, directly or indirectly;

(b) The terms and conditions of the financing are acceptable to SBA;

(c) The source is not the Borrower or an Associate of the Borrower; and

(d) The source has the experience and qualifications to monitor properly all Project construction and progress payments. (If the source lacks such experience or qualifications, SBA may require the interim loan to be managed by a third party such as a bank or professional construction manager.)

§ 120.891 Certifications of disbursement and completion.

Before the Debenture is issued, the interim lender must certify the amount disbursed. The CDC must certify that the Project was completed in accordance with the final plans and specifications (except as provided in § 120.961).

§ 120.892 Certifications of no adverse change.

Following completion of the Project, the following certifications must be made before the 504 loan closing:

(a) The interim lender must certify to the CDC that it has no knowledge of any unremedied substantial adverse change in the condition of the small business since the application to the interim lender;

(b) The Borrower (or Operating Company) must certify to the CDC that there has been no unremedied substantial adverse change in its financial condition or its ability to repay the 504 loan since the date of application, and must furnish interim financial statements, current within 120 days of closing; and

(c) The CDC must issue an opinion to the best of its knowledge that there has been no unremedied substantial adverse change in the Borrower's (or Operating Company's) ability to repay

the 504 loan since its submission of the loan application to SBA.

[61 FR 3235, Jan. 31, 1996, as amended at 68 FR 57987, Oct. 7, 2003]

PERMANENT FINANCING

§ 120.900 Sources of permanent financing.

Permanent financing for each Project must come from three sources: the Borrower's contribution, Third-Party Loans, and the 504 loan. Typically, the Borrower contributes 10 percent of the permanent financing, Third-Party Loans 50 percent and the 504 loan 40 percent.

THE BORROWER'S CONTRIBUTION

§ 120.910 Borrower contributions.

(a) The Borrower must contribute to the Project cash (or property acceptable to SBA obtained with the cash) or land (that is part of the Project Property), in an amount equal to the following percentage of the Project cost, excluding administrative costs:

(1) At least 15 percent, if the Borrower (or Operating Company if the Borrower is an Eligible Passive Company) has operated for two years or less;

(2) At least 15 percent, if the Project involves the acquisition, construction, conversion, or expansion of a limited or single purpose building or structure;

(3) At least 20 percent, if the Project involves conditions described in paragraphs (a)(1) and (2) of this section; or

(4) At least 10 percent, in all other circumstances.

(b) The source of the contribution may be a CDC or any other source except an SBA business loan program (see § 120.913 for SBIC exception).

[64 FR 2118, Jan. 13, 1999]

§ 120.911 Land contributions.

The Borrower's contribution may be land (including buildings, structures and other site improvements which will be part of the Project Property) previously acquired by the Borrower.

[68 FR 57987, Oct. 7, 2003]

§ 120.912 Borrowed contributions.

The Borrower may borrow its cash contribution from the CDC or a third party. If any of the contribution is borrowed, the interest rate must be reasonable. If the loan is secured by any of the Project assets, the loan must be subordinate to the liens securing the 504 Loan, and the loan may not be repaid at a faster rate than the 504 Loan unless SBA gives prior written approval. A third party lender may not receive voting rights, stock options, or any other actual or potential voting interest in the small business.

§ 120.913 Limitations on any contributions by a Licensee.

Subject to part 107 of this chapter, a Licensee may provide financing for all or part of the Borrower's contribution to the Project. SBA will consider Licensee funds to be derived from federal sources if the Licensee has Leverage (as defined in § 107.50 of this chapter). If the Licensee does not have Leverage, SBA will consider the investment to be from private funds. Licensee financing must be subordinated to the 504 loan and must not be repaid at a faster rate than the Debenture. (Refer to § 120.930(a) for additional limitations.)

[68 FR 57987, Oct. 7, 2003]

THIRD PARTY LOANS

§ 120.920 Required participation by the Third Party Lender.

(a) *Amount of Third Party Loans.* A Project financing must include one or more Third Party Loans totaling at least as much as the 504 loan. However, the Third Party Loans must total at least 50 percent of the total cost of the Project if:

(1) The Borrower (or Operating Company, if the Borrower is an Eligible Passive Company) has operated for two years or less, or

(2) The Project is for the acquisition, construction, conversion or expansion of a limited or single purpose asset.

(b) *Third party loan collateral.* The 504 loan is usually collateralized by a second lien on Project Property. The Third Party Lender may obtain additional collateral or other security for

the Third Party Loan (''Additional Collateral'') only if in the event of liquidation and unless otherwise approved in writing by SBA:

(1) The Third Party Lender liquidates or otherwise exhausts all reasonable avenues of collection with respect to the Additional Collateral no later than the disposition of the Project Property, and

(2) The Third Party Lender applies any proceeds received as a result of the Additional Collateral to the balance outstanding on the Third Party Loan prior to the application of proceeds from the disposition of the Project Property to the Third Party Loan.

[64 FR 2118, Jan. 13, 1999, as amended at 79 FR 15650, Mar. 21, 2014]

§ 120.921 Terms of Third Party loans.

(a) *Maturity*. A Third Party Loan must have a term of at least 7 years when the 504 loan is for a term of 10 years and 10 years when the 504 loan is for 20 years. If there is more than one Third Party Loan, an overall loan maturity must be calculated, taking into account the maturities and amounts of each loan. If there is a balloon payment, it must be justified in the loan report and clearly identified in the Loan Authorization.

(b) *Interest rates*. Interest rates must be reasonable. SBA must establish and publish in the FEDERAL REGISTER a maximum interest rate for any Third Party Loan from commercial financial institutions. The rate shall remain in effect until changed.

(c) *Other terms*. The Third Party Loan must not have any early call feature or contain any demand provisions unless the loan is in default. By participating, a Third Party Loan lender waives, as to the CDC/SBA financing, any provision in its deed of trust, or mortgage, or other documents prohibiting further encumbrances or subordinate debt. In the event of default, the Third Party Lender must give the CDC and SBA written notice of default within 30 days of the event of default and at least 60 days prior to foreclosure.

(d) *Future advances*. The Third Party Loan must not be open-ended. After completion of the Project, the Third Party Lender may not make future advances under the Third Party Loan except expenditures to collect amounts due the Third Party Loan notes, maintain collateral and protect the Third Party Lender's lien position on the Third Party Loan.

(e) *Subordination*. The Third Party Lender's lien will be subordinate to the CDC/SBA lien regarding any prepayment penalties, late fees, other default charges, and escalated interest after default due under the Third Party Loan.

(f) *Escalation upon default*. A Third-Party Lender may not escalate the rate of interest upon default to a rate greater than the maximum rate set forth in paragraph (b) of this section. Regarding any Project that SBA approved after September 30, 1996, SBA will only pay the interest rate on the note in effect before the date of the Borrower's default.

[61 FR 3235, Jan. 31, 1996, as amended at 64 FR 2118, Jan. 13, 1999]

§ 120.922 Pre-existing debt on the Project Property.

In addition to its share of Project cost, a Third-Party Loan may include consolidation of existing debt on the Project Property. The consolidation must not improve the lien position of the Lender on the pre-existing debt, unless the debt is a previous Third-Party Loan.

§ 120.923 Policies on subordination.

(a) Financing provided by the seller of Project Property must be subordinate to the 504 loan. SBA may waive the subordination requirement if the property is classified as ''other real estate owned'' by a national bank or other Federally regulated lender and SBA considers the property to be of sufficient value to support the 504 loan.

(b) A Borrower is eligible for a 504 loan even if part of the Project financing is tax-exempt. SBA's lien position must not be subordinate to loans made from the proceeds of the tax-exempt obligation.

(c) The Borrower must not prepay any Project financing subordinate to the 504 loan without SBA's prior written consent.

[61 FR 3235, Jan. 31, 1996, as amended at 68 FR 57988, Oct. 7, 2003]

§ 120.925 [Reserved]

§ 120.926 Referral fee.

The CDC can receive a reasonable referral fee from the Third Party Lender if the CDC secured the Third Party Lender for the Borrower under a written contract between the CDC and the Third Party Lender. Both the CDC and the Third Party Lender are prohibited from charging this fee to the Borrower. If a CDC charges a referral fee, the CDC will be construed as a Referral Agent under part 103 of this chapter.

[68 FR 57988, Oct. 7, 2003]

504 LOANS AND DEBENTURES

§ 120.930 Amount.

(a) Generally, a 504 loan may not exceed 40 percent of total Project cost plus 100 percent of eligible administrative costs. For good cause shown, SBA may authorize an increase in the percentage of Project costs covered up to 50 percent. No more than 50 percent of eligible Project costs can be from Federal sources, whether received directly or indirectly through an intermediary.

(b) A 504 loan must not be less than $25,000.

(c) Upon completion of the Project, the Debenture amount will be reduced by the amount that the unused contingency reserve exceeds 2 percent of the anticipated Debenture.

[61 FR 3235, Jan. 31, 1996, as amended at 68 FR 57988, Oct. 7, 2003]

§ 120.931 504 Lending limits.

504 loan amounts shall be limited to:

(a) An outstanding balance of $5,000,000 for each Borrower and its affiliates if the loan proceeds will not be directed towards a Project in paragraph (c) of this section,

(b) An outstanding balance of $5,000,000 for each Borrower and its affiliates if one or more of the public policy goals enumerated in §120.862(b) applies to the Project; and

(c) $5,500,000 for each Project for:

(1) Small Manufacturers (NAICS Codes 31–33) with all production facilities located in the United States;

(2) Reduction of the Borrower's, or if the Borrower is an Eligible Passive Company, the Operating Company's energy consumption by at least 10%; or

(3) Plant, equipment and process upgrades of renewable energy sources such as the small-scale production of energy for individual buildings' or communities' consumption, commonly known as micropower, or renewable fuel producers including biodiesel and ethanol producers.

[76 FR 63547, Oct. 12, 2011]

§ 120.932 Interest rate.

The interest rate of the 504 Loan and the Debenture which funds it is set by the SBA and approved by the Secretary of the Treasury.

§ 120.933 Maturity.

From time to time, SBA will publish in the FEDERAL REGISTER the available maturities for a 504 loan and the Debenture that funds it. Such available maturities remain in effect until changed by subsequent FEDERAL REGISTER publication.

[68 FR 57988, Oct. 7, 2003]

§ 120.934 Collateral.

The CDC usually takes a second lien position on the Project Property to secure the 504 loan. Sometimes additional collateral is required. (In rare circumstances, SBA may permit other collateral substituted for Project Property.) All collateral must be insured against such hazards and risks as SBA may require, with provisions for notice to SBA and the CDC in the event of impending lapse of coverage.

[68 FR 57988, Oct. 7, 2003]

§ 120.935 Deposit from the Borrower that a CDC may require.

At the time of application for a 504 loan, the CDC may require a deposit from the Borrower of $2,500 or 1 percent of the Net Debenture Proceeds, whichever is less. The deposit may be applied to the loan processing fee if the application is accepted, but must be refunded if the application is denied. If the small business withdraws its application, the CDC may deduct from the deposit reasonable costs incurred in packaging and processing the application.

§ 120.937 Assumption.

A 504 loan may be assumed with SBA's prior written approval.

§ 120.938 Default.

(a) Upon occurrence of an event of default specified in the 504 note which requires automatic acceleration, the note becomes due and payable. Upon occurrence of an event of default which does not require automatic acceleration, SBA may forbear acceleration of the note and attempt to resolve the default. If the default is not cured subsequently, the note shall be accelerated. In either case, upon acceleration of the note, the Debenture which funded it is also due immediately, and SBA must honor its guarantee of the Debenture. SBA shall not reimburse the investor for any premium paid.

(b) If a CDC defaults on a Debenture, SBA generally shall limit its recovery to the payments made by the small business to the CDC on the loan made from the Debenture proceeds, and the collateral securing the defaulted loan. However, SBA will look to the CDC for the entire amount of the Debenture in the case of fraud, negligence, or misrepresentation by the CDC.

§ 120.939 Borrower prohibition.

Neither a Borrower nor an Associate of the Borrower may purchase an interest in a Debenture Pool in which the Debenture that funded its 504 loan has been placed.

§ 120.940 Prepayment of the 504 loan or Debenture.

The Borrower may prepay its 504 loan, if it pays the entire principal balance, unpaid interest, any unpaid fees, and any prepayment premium established in the note. If the Borrower prepays, the CDC must prepay the corresponding Debenture with interest and premium. If one of the Debentures in a Debenture Pool is prepaid, the Investors in that Debenture Pool must be paid pro rata, and SBA's guarantee on the entire Debenture Pool must be proportionately reduced. If the entire Debenture Pool is paid off, SBA may call all Certificates backed by the Pool for redemption.

§ 120.941 Certificates.

(a) The face value of a Certificate must be at least $25,000. Certificates are issued in registered form and transferred only by entry on the central registry maintained by the Trustee. SBA guarantees the timely payment of principal and interest on the Certificates.

(b) Before the sale of a Certificate, the seller, or the broker or dealer acting as the seller's agent, must disclose to the purchaser the terms, conditions, yield, and premium and other characteristics not guaranteed by SBA.

Debenture Sales and Service Agents

§ 120.950 SBA and CDC must appoint agents.

SBA and the CDC must appoint the following agents to facilitate the sale and service of the Certificates and disbursement of the proceeds.

§ 120.951 Selling agent.

The CDC, with SBA approval, shall appoint a Selling Agent to select underwriters, negotiate the terms and conditions of Debenture offerings with the underwriters, and direct and coordinate Debenture sales.

§ 120.952 Fiscal agent.

SBA shall appoint a Fiscal Agent to assess the financial markets, minimize the cost of sales, arrange for the production of the Offering Circular, Debenture Certificates, and other required documents, and monitor the performance of the Trustee and the underwriters.

§ 120.953 Trustee.

SBA must appoint a Trustee to:

(a) Issue Certificates;

(b) Transfer the Certificates upon resale in the secondary market;

(c) Maintain physical possession of the Debentures for SBA and the Certificate holders;

(d) Establish and maintain a central registry of:

(1) Debenture Pools, including the CDC obligors and the interest rate payable on the Debentures in each Pool;

(2) Certificates issued or transferred, including the Debenture Pool backing the Certificate, name and address of the purchaser, price paid, the interest

rate on the Certificate, and fees or charges assessed by the transferror; and

(3) Brokers and dealers in Certificates, and the commissions, fees or discounts granted to the brokers and dealers;

(e) Receive semi-annual Debenture payments and prepayments;

(f) Make regularly scheduled and prepayment payments to Investors; and

(g) Assure before any resale of a Debenture or Certificate is recorded in the registry that the seller has provided the purchaser a written disclosure statement approved by SBA.

§ 120.954 Central Servicing Agent.

(a) SBA has entered into a Master Servicing Agreement designating a Central Servicing Agent (CSA) to support the orderly flow of funds among Borrowers, CDCs, and SBA. The CDC and Borrower must enter into an individual Servicing Agent Agreement with the CSA for each 504 loan, constituting acceptance by the CDC and the Borrower of the terms of the Master Servicing Agreement.

(b) The CSA has established a master reserve account. All funds related to the 504 loans and Debentures flow through the master reserve account under the provisions of the Master Servicing Agreement. The master reserve account will be funded by a guarantee fee, a funding fee to be published from time to time in the FEDERAL REGISTER, and by principal and interest payments of 504 loans. At SBA's direction, the CSA may use funds in the master reserve account to defray program expenses. In the event a Borrower defaults and its 504 note is accelerated, SBA shall add funds under its guarantee to ensure the full and timely payment of the Debenture which funded the 504 loan. At SBA's direction, the CSA must pay to the CDC servicing each loan the interest accruing in the master reserve account on loan payments made by each Borrower between the date of receipt of each monthly payment and the date of disbursement to investors. The CSA may disburse such interest periodically to CDCs on a pro rata basis. SBA may use interest accruals in the master reserve account earned prior to October 1991 (not previously distributed to the CDCs) for the costs of 504 program administration.

§ 120.955 Agent bonds and records.

(a) Each agent (in §§ 120.951 through 120.954) must provide a fidelity bond or insurance in such amount as necessary to fully protect the interest of the government.

(b) SBA must have access at the agent's place of business to all books, records and other documents relating to Debenture activities.

§ 120.956 Suspension or revocation of brokers and dealers.

The appropriate Office of Capital Access official in accordance with Delegations of Authority may suspend or revoke the privilege of any broker or dealer to participate in the sale or marketing of Debentures and Certificates for actions or conduct bearing negatively on the broker's fitness to participate in the securities market. SBA must give the broker or dealer written notice, stating the reasons, at least 10 business days prior to the effective date of the suspension or revocation. A broker or dealer may appeal the suspension or revocation made under this section pursuant to the procedures set forth in part 134 of this chapter. The action of this official will remain in effect pending resolution of the appeal.

[73 FR 75519, Dec. 11, 2008]

CLOSINGS

§ 120.960 Responsibility for closing.

(a) The CDC is responsible for the 504 loan closing.

(b) The Debenture closing is the joint responsibility of the CDC and SBA.

(c) SBA may, within its sole discretion, decline to close the Debenture; direct the transfer of the 504 loan to another CDC; or cancel its guarantee of the Debenture, prior to sale, if any of the following occur:

(1) The CDC has failed to comply materially with any requirement imposed by statute, regulation, SOP, policy and procedural notice, any agreement the CDC has executed with SBA, or the terms of a Debenture or loan authorization;

(2) The CDC has failed to make or close the 504 loan or prepare the Debenture closing in a prudent or commercially reasonable manner;

(3) The CDC's improper action or inaction places SBA at risk;

(4) The CDC has failed to use required SBA forms or electronic versions of those forms;

(5) The CDC, Third Party Lender or Borrower has failed to timely disclose to SBA a material fact regarding the Project or 504 loan;

(6) The CDC, Third Party Lender or Borrower has misrepresented a material fact to SBA regarding the Project or 504 loan; or

(7) SBA determines that there has been an unremedied material adverse change, such as deterioration in the Borrower's financial condition, since the 504 loan was approved, or that approving the closing of the Debenture will put SBA at unacceptable financial risk.

[68 FR 57988, Oct. 7, 2003]

§ 120.961 Construction escrow accounts.

The CSA, title company, CDC attorney, or bank may hold Debenture proceeds in escrow to complete Project components such as landscaping and parking lots, and acquire machinery and equipment if the component or acquisition is a minor portion of the total Project and has been contracted for completion or delivery at a specified price and specific future date. The escrow agent must disburse funds upon approval by the CDC and the SBA, supported by invoices and payable jointly to the small business and the designated contractor.

SERVICING

§ 120.970 Servicing of 504 loans and Debentures.

(a) In servicing 504 loans, CDCs must comply with Loan Program Requirements and in accordance with prudent and commercially reasonable lending standards.

(b) The CDC is responsible for routine servicing including receipt and review of the Borrower's or Operating Company's financial statements on an annual or more frequent basis and monitoring the status of the Borrower and 504 loan collateral.

(c) The CDC is responsible for assuring that the Borrower makes all required insurance premium payments and has paid all taxes when due.

(d) The CDC is responsible for filing renewals and extensions of security interests on collateral for the 504 loan, as required.

(e) The CDC must timely respond to Borrower requests for loan modifications.

(f) For any 504 loan that is more than three months past due, the CDC must promptly request that SBA purchase the Debenture unless the 504 loan has an SBA-approved deferment or is in compliance with an SBA-approved plan to allow the Borrower to catch up on delinquent loan payments.

(g) The CDC must cooperate with SBA to cure defaults and initiate workouts.

(h) Additional servicing requirements are set forth in subpart E of this part.

[68 FR 57988, Oct. 7, 2003, as amended at 72 FR 18364, Apr. 12, 2007]

FEES

§ 120.971 Allowable fees paid by Borrower.

(a) *CDC fees.* The fees a CDC may charge the Borrower in connection with a 504 loan and Debenture are limited to the following:

(1) *Processing fee.* The CDC may charge up to 1.5 percent of the net Debenture proceeds to process the financing. Two-thirds of this fee will be considered earned and may be collected by the CDC when the Authorization for the Debenture is issued by SBA. The portion of the processing fee paid by the Borrower may be reimbursed from the Debenture proceeds;

(2) *Closing fee.* The CDC may charge a reasonable closing fee sufficient to reimburse it for the expenses of its in-house or outside legal counsel, and other miscellaneous closing costs (CDC Closing Fee). Some closing costs may be funded out of the Debenture proceeds (see § 120.883 for limitations);

(3) *Servicing fee.* The CDC will charge a monthly servicing fee of at least 0.625 percent per annum and no more than 2

percent per annum on the unpaid balance of the loan as determined at five-year anniversary intervals. A servicing fee greater than 1.5 percent in a rural area and 1 percent everywhere else requires SBA's prior written approval, based on evidence of substantial need. The servicing fee may be paid only from loan payments received. The fees may be accrued without interest and collected from the CSA when the payments are made.

(4) *Late fees.* Loan payments received after the 15th of each month may be subject to a late payment fee of 5 percent of the late payment or $100, whichever is greater. These fees will be collected by the CSA on behalf of the CDC; and

(5) *Assumption fee.* Upon SBA's written approval, a CDC may charge an assumption fee not to exceed 1 percent of the outstanding principal balance of the loan being assumed.

(b) *CSA fees.* The CSA may charge an initiation fee on each loan and a monthly servicing fee under the terms of the Master Servicing Agreement.

(c) *Other agent fees.* Agent fees and charges necessary to market and service Debentures and Certificates may be assessed to the Borrower or the investor. The fees must be approved by SBA and published periodically in the FEDERAL REGISTER.

(d) *SBA fees.* (1) SBA charges a 0.5 percent guarantee fee on the Debenture.

(2) For loans approved by SBA after September 30, 1996, SBA charges a fee of not more than 0.9375 percent annually on the unpaid principal balance of the loan as determined at five-year anniversary intervals.

(e) *Miscellaneous fees.* A funding fee not to exceed 0.25 percent of the Debenture may be charged to cover costs incurred by the trustee, fiscal agent, transfer agent.

[61 FR 3235, Jan. 31, 1996, as amended at 64 FR 2119, Jan. 13, 1999; 68 FR 57988, Oct. 7, 2003]

§ 120.972 Third Party Lender participation fee and CDC fee.

(a) *Participation fee.* For loans approved by SBA after September 30, 1996, SBA must collect a one-time fee equal to 50 basis points on the Third Party Lender's participation in a Project when the Third Party Lender occupies a senior credit position to SBA in the Project.

(b) *CDC fee.* For loans approved by SBA after September 30, 1996, SBA must collect an annual fee from the CDC equal to 0.125 percent of the outstanding principal balance of the Debenture. The fee must be paid from the servicing fees collected by the CDC and cannot be paid from any additional fees imposed on the Borrower.

[68 FR 57988, Oct. 7, 2003]

AUTHORITY OF CDCS TO PERFORM LIQUIDATION AND DEBT COLLECTION LITIGATION

§ 120.975 CDC Liquidation of loans and debt collection litigation.

(a) *PCLP CDCs.* If a CDC is designated as a PCLP CDC under § 120.845, the CDC must liquidate and handle debt collection litigation with respect to all PCLP Loans in its portfolio on behalf of SBA as required by § 120.848(f), in accordance with subpart E of this part. With respect to all other 504 loans that a PCLP CDC makes, the PCLP CDC is an Authorized CDC Liquidator and must exercise its delegated authority to liquidate and handle debt-collection litigation in accordance with subpart E of this part for such loans, if the PCLP CDC is notified by SBA that it meets either of the following requirements to be an Authorized CDC Liquidator, as determined by SBA:

(1) The PCLP CDC has one or more employees who have not less than two years of substantive, decision-making experience in administering the liquidation and workout of defaulted or problem loans secured in a manner substantially similar to loans funded with 504 loan program debentures, and who have completed a training program on loan liquidation developed by the Agency in conjunction with qualified CDCs that meet the requirements of this section; or

(2) The PCLP CDC has entered into a contract with a qualified third party for the performance of its liquidation responsibilities and obtains the approval of SBA with respect to the qualifications of the contractor and the terms and conditions of the contract.

(b) *All other CDCs.* A CDC that is not authorized under paragraph (a) of this section may apply to become an Authorized CDC Liquidator with authority to liquidate and handle debt collection litigation with respect to 504 loans on behalf of SBA, in accordance with subpart E of this part, if the CDC meets the following requirements:

(1) The CDC meets either of the following criteria:

(i) The CDC participated in the loan liquidation pilot program established by the Small Business Programs Improvement Act of 1996 prior to October 1, 2006; or

(ii) During the three fiscal years immediately prior to seeking such authority, the CDC made an average of not less than ten 504 loans per year; and

(2) The CDC meets either of the following requirements:

(i) The CDC has one or more employees who have not less than two years of substantive, decision-making experience in administering the liquidation and workout of defaulted or problem loans secured in a manner substantially similar to loans funded with 504 loan program debentures, and who have completed a training program on loan liquidation developed by the Agency in conjunction with qualified CDCs that meet the requirements of this section; or

(ii) The CDC has entered into a contract with a qualified third party for the performance of its liquidation responsibilities and obtains the approval of SBA with respect to the qualifications of the contractor and the terms and conditions of the contract.

(c) *CDC counsel.* To perform debt collection litigation under paragraphs (a) or (b) of this section, a CDC must also have either in-house counsel with adequate experience as approved by SBA or entered into a contract for the performance of debt collection litigation with an experienced attorney or law firm as approved by SBA.

(d) *Application for authority to liquidate and litigate.* To seek authority to perform liquidation and debt collection litigation under paragraphs (b) and (c) of this section, a CDC other than a PCLP CDC must submit a written application to SBA and include documentation demonstrating that the CDC meets the requirements of paragraph (b) and (c) of this section. If a CDC intends to use a contractor to perform liquidation, it must obtain approval from SBA of both the qualifications of the contractor and the terms and conditions in the contract covering the CDC's retention of the contractor. SBA will notify a CDC in writing when the CDC can begin to perform liquidation and/or debt collection litigation under this section.

[72 FR 18365, Apr. 12, 2007]

ENFORCEABILITY OF 501, 502 AND 503 LOANS AND OTHER LAWS

§ 120.990 501, 502 and 503 loans.

SBA has discontinued loan programs for 501, 502, and 503 loans. Outstanding loans remain under these programs, and Borrowers, CDCs, and SBA must comply with the terms and conditions of the corresponding notes and Debentures, and the regulations in this part in effect when the obligations were undertaken or last in effect, if applicable.

§ 120.991 Effect of other laws.

No State or local law may preclude or limit SBA's exercise of its rights with respect to notes, guarantees, Debentures and Debenture Pools, or of its enforcement rights to foreclose on collateral.

Subpart I—Risk-Based Lender Oversight

SOURCE: 72 FR 25194, May 4, 2007, unless otherwise noted.

SUPERVISION

§ 120.1000 Risk-Based Lender Oversight.

(a) *Risk-Based Lender Oversight.* SBA supervises, examines, and regulates, and enforces laws against, SBA Supervised Lenders and the SBA operations of SBA Lenders, Intermediaries, and NTAPs.

(b) *Scope.* Most rules and standards set forth in this subpart apply to SBA Lenders as well as Intermediaries and NTAPs, However, SBA has separate regulations for enforcement grounds

and enforcement actions for Intermediaries and NTAPs at §120.1425 and §120.1540.

[73 FR 75519, Dec. 11, 2008]

§120.1005 Bureau of PCLP Oversight.

SBA's Bureau of PCLP Oversight within OCRM, monitors the capitalization of PCLP CDC pilot participants' LLRFs and performs other related functions.

[73 FR 75519, Dec. 11, 2008]

§120.1010 SBA access to SBA Lender, Intermediary, and NTAP files.

An SBA Lender, Intermediary, and NTAP must allow SBA's authorized representatives, including representatives authorized by the SBA Inspector General, during normal business hours, access to its files to review, inspect, and copy all records and documents, relating to SBA guaranteed loans or as requested for SBA oversight.

[73 FR 75519, Dec. 11, 2008]

§120.1015 Risk Rating System.

(a) *Risk Rating*. SBA may assign a Risk Rating to all SBA Lenders, Intermediaries, and NTAPs on a periodic basis. Risk Ratings are based on certain risk-related portfolio performance factors as set forth in notices or SBA's SOPs and as published from time to time.

(b) *Rating categories*. Risk Ratings fall into one of two broad categories: Acceptable Risk Ratings or Less Than Acceptable Risk Ratings.

[73 FR 75519, Dec. 11, 2008]

§120.1025 Monitoring.

SBA may conduct monitoring of SBA Lenders, Intermediaries, and NTAPs, including SBA Lenders', Intermediaries' or NTAPs' self-assessments.

[73 FR 75519, Dec. 11, 2008, as amended at 82 FR 39504, Aug. 21, 2017]

§120.1050 Reviews and examinations.

(a) *Reviews*. SBA may conduct reviews of the SBA loan operations of SBA Lenders. The review may include, but is not limited to, an evaluation of the following:

(1) Portfolio performance;

(2) SBA operations management;

(3) Credit administration; and

(4) Compliance with Loan Program Requirements.

(b) *Examinations*. SBA may conduct safety and soundness examinations of SBA Supervised Lenders, except SBA will not conduct safety and soundness examinations of Other Regulated SBLCs under §§120.1510 and 1511. The safety and soundness examination may include, but is not limited to, an evaluation of:

(1) Capital adequacy;

(2) Asset quality (including credit administration and allowance for loan losses);

(3) Management quality (including internal controls, loan portfolio management, and asset/liability management);

(4) Earnings;

(5) Liquidity; and

(6) Compliance with Loan Program Requirements.

(c) *Reviews/examinations of Intermediaries and NTAPs*. SBA may perform reviews or examinations of Intermediaries and NTAPs.

(d) *Other reviews or examinations*. SBA may perform other reviews/examinations as needed as determined by SBA in its discretion.

[73 FR 75519, Dec. 11, 2008, as amended at 82 FR 39504, Aug. 21, 2017]

§120.1051 Frequency of reviews and examinations.

SBA may conduct reviews and examinations of SBA Lenders, Intermediaries, and NTAPs on a periodic basis. SBA may consider, but is not limited to, the following factors in determining frequency:

(a) Results of monitoring, including an SBA Lender's, Intermediary's or NTAP's Risk Rating;

(b) SBA loan portfolio size;

(c) Previous review or examination findings;

(d) Responsiveness in correcting deficiencies noted in prior reviews or examinations; and

(e) Such other risk-related information as SBA, in its discretion, determines to be appropriate.

[73 FR 75519, Dec. 11, 2008, as amended at 82 FR 39504, Aug. 21, 2017]

§ 120.1055 Review and examination results.

(a) *Written Reports.* SBA will provide an SBA Lender, Intermediary, and NTAP a copy of SBA's written report prepared as a result of the SBA Lender review or examination (''Report''). The Report may contain findings, conclusions, corrective actions and recommendations. Each director (or manager, in the absence of a Board of Directors) of the SBA Lender, Intermediary, and NTAP, in keeping with his or her responsibilities, must become fully informed regarding the contents of the Report.

(b) *Response to review and examination Reports.* SBA Lenders, Intermediaries, and NTAPs must respond to Report findings and corrective actions, if any, in writing to SBA and, if requested, submit proposed corrective actions and/or a capital restoration plan. An SBA Lender, Intermediary, or NTAP must respond within 30 days from the Report date unless SBA notifies the SBA Lender, Intermediary, or NTAP in writing that the response, proposed corrective actions or capital restoration plan is to be filed within a different time period. The SBA Lender, Intermediary, or NTAP response must address each finding and corrective action. In proposing a corrective action or capital restoration plan, the SBA Lender, Intermediary, or NTAP must detail: The steps it will take to correct the finding(s); the time within which each step will be taken; the timeframe for accomplishing the entire corrective action plan; and the person(s) or department at the SBA Lender, Intermediary, or NTAP charged with carrying out the corrective action or capital restoration plan, as applicable.

(c) *SBA response.* SBA will provide written notice of whether the response and, if applicable, any corrective action or capital restoration plan, is approved, or whether SBA will seek additional information or require other action.

(d) *Failure to respond or to submit or implement an acceptable plan.* If an SBA Lender, Intermediary, or NTAP fails to respond in writing to SBA, respond timely to SBA, or provide a response acceptable to SBA within SBA's discretion, or respond to all findings and required corrective actions in a Report, then SBA may take enforcement action under Subpart I. If an SBA Lender, Intermediary, or NTAP that is requested to submit a corrective action plan or capital restoration plan to SBA fails to do so in writing; fails to submit timely such plan to SBA; or fails to submit a plan acceptable to SBA within SBA's discretion, then SBA may take enforcement action under § 120.1500 through § 120.1540. If an SBA Lender, Intermediary, or NTAP fails to implement in any material respect a corrective action or capital restoration plan within the required timeframe, then SBA may undertake enforcement action under § 120.1500 through § 120.1540.

[73 FR 75519, Dec. 11, 2008]

§ 120.1060 Confidentiality of Reports, Risk Ratings and related Confidential Information.

(a) *In general.* Reports and other SBA prepared review or examination related documents are the property of SBA and are loaned to an SBA Lender, Intermediary, or NTAP for its confidential use only. The Reports, Risk Ratings, and related Confidential Information are privileged and confidential as more fully explained in paragraph (b) of this section. The Report, Risk Rating, and Confidential Information must not be relied upon for any purpose other than SBA's Lender oversight and SBA's portfolio management purposes. An SBA Lender, Intermediary, or NTAP must not make any representations concerning the Report (including its findings, conclusions, and recommendations), the Risk Rating, or the Confidential Information. For purposes of this regulation, Report means the review or examination report and related documents. For purposes of this regulation, Confidential Information is defined in the SBA Lender information portal and by notice issued from time to time. Access to the Lender information portal may be obtained by contacting the OCRM.

(b) *Disclosure prohibition.* Each SBA Lender, Intermediary, and NTAP is prohibited from disclosing its Report, Risk Rating, and Confidential Information, in full or in part, in any manner,

without SBA's prior written permission. An SBA Lender, Intermediary, and NTAP may use the Report, Risk Rating, and Confidential Information for confidential use within its own immediate corporate organization. SBA Lenders, Intermediaries, and NTAPs must restrict access to their Report, Risk Rating and Confidential Information to their respective parent entities, officers, directors, employees, auditors and consultants, in each case who demonstrate a legitimate need to know such information for the purpose of assisting in improving the SBA Lender's, Intermediary's, or NTAP's SBA program operations in conjunction with SBA's Program and SBA's portfolio management (for purposes of this regulation, each referred to as a ''permitted party''), and to those for whom SBA has approved access by prior written consent, and those for whom access is required by applicable law or legal process. If such law or process requires SBA Lender, Intermediary, or NTAP to disclose the Report, Risk Rating, or Confidential Information to any person other than a permitted party, SBA Lender, Intermediary, or NTAP will promptly notify SBA and SBA's Information Provider in writing and in advance of such disclosure so that SBA and the Information Provider have, within their discretion, the opportunity to seek appropriate relief such as an injunction or protective order prior to disclosure. For purposes of this regulation, ''consultants'' means only those consultants that are under written contract with an SBA Lender, Intermediary or NTAP specifically to assist with addressing its Report Findings and Corrective Actions to SBA's satisfaction. The consultant contract must provide for both the consultant's agreement to abide by the disclosure prohibition in this paragraph and the consultant's agreement not to use the Report, Risk Rating, and Confidential Information for any purpose other than to assist with addressing the Report Findings and Corrective Actions. ''Information Provider'' means any contractor that provides SBA with the Risk Rating. Each SBA Lender, Intermediary, and NTAP must ensure that each permitted party is aware of and agrees to these regulatory requirements and must ensure that each such permitted party abides by them. Any disclosure of the Report, Risk Rating, or Confidential Information other than as permitted by this regulation may result in appropriate action as authorized by law. An SBA Lender, Intermediary, and NTAP will indemnify and hold harmless SBA from and against any and all claims, demands, suits, actions, and liabilities to any degree based upon or resulting from any unauthorized use or disclosure of the Report, Risk Rating, or Confidential Information. Information Provider contact information is available from the Office of Capital Access.

[73 FR 75519, Dec. 11, 2008, as amended at 82 FR 39504, Aug. 21, 2017]

§ 120.1070 SBA Lender oversight fees.

Lenders are required to pay to SBA fees to cover costs of examinations and reviews and, if assessed by SBA, other Lender oversight activities.

(a) *Fee components:* The fees may cover the following:

(1) *Examinations.* The costs of conducting a safety and soundness examination and related activities of an SBA-Supervised Lender, including any expenses that are incurred in relation to the examination and such activities.

(2) *Reviews.* The costs of conducting a review of a 7(a) Lender or a 7(a) Lender's loans, and related review activities (*e.g.*, corrective action assessments, delegated loan reviews), including any expenses that are incurred in relation to the review and such activities.

(3) *Monitoring.* The costs of conducting monitoring reviews of a 7(a) Lender, including any expenses that are incurred in relation to the monitoring review activities.

(4) *Other lender oversight activities.* The costs of additional expenses that SBA incurs in carrying out other lender oversight activities (for example, the salaries and travel expenses of SBA employees and equipment expenses that are directly related to carrying out lender oversight activities, technical assistance and analytics to support the monitoring and review program, and supervision and enforcement activity costs).

(b) *Allocation.* SBA will assess to 7(a) Lender(s) the costs associated with the

review, examination, monitoring, or other lender oversight activity, as determined by SBA in its discretion. In general:

(1) Where the costs that SBA incurs for a review, exam, monitoring or other lender oversight activity are specific to a particular 7(a) Lender, SBA will charge that 7(a) Lender a fee for the actual costs of conducting the review, exam, monitoring or other lender oversight activity; and

(2) Where the costs that SBA incurs for the lender oversight activity are not sufficiently specific to a particular Lender, SBA will assess a fee based on each 7(a) Lender's portion of the total dollar amount of SBA guarantees in SBA's total portfolio or in the relevant portfolio segment being reviewed or examined, to cover the costs of such activity. SBA may waive the assessment of this fee for all 7(a) Lenders owing less than a threshold amount below which SBA determines that it is not cost effective to collect the fee.

(c) *Billing process.* For the examinations or reviews conducted under paragraphs (a)(1) and (2) of this section, SBA will bill each 7(a) Lender for the amount owed following completion of the examination, review or related activity. For monitoring conducted under paragraph (a)(3) of this section and the other lender oversight activity expenses incurred under paragraph (a)(4) of this section, SBA will bill each 7(a) Lender for the amount owed on an annual basis. SBA will state in the bill the date by which payment is due SBA and the approved payment method(s). The payment due date will be no less than 30 calendar days from the bill date.

(d) *Delinquent payment and late-payment charges.* Payments that are not received by the due date specified in the bill shall be considered delinquent. SBA will charge interest, and other applicable charges and penalties, on delinquent payments, as authorized by 31 U.S.C. 3717. SBA may waive or abate the collection of interest, charges and/or penalties if circumstances warrant. In addition, a 7(a) Lender's failure to pay any of the fee components described in this section, or to pay interest, charges and penalties that have been charged, may result in a decision to suspend or revoke a participant's eligibility, limit a participant's delegated authority, or other remedy available under law.

[61 FR 3235, Jan. 31, 1996, as amended at 82 FR 39505, Aug. 21, 2017]

ENFORCEMENT ACTIONS

§ 120.1400 Grounds for enforcement actions—SBA Lenders.

(a) *Agreements.* By making SBA 7(a) guaranteed loans or 504 loans, SBA Lenders automatically agree to the terms, conditions, and remedies in Loan Program Requirements, as promulgated or issued from time to time and as if fully set forth in the SBA Form 750 (Loan Guaranty Agreement), Development Company 504 Debenture, CDC Certification, Servicing Agent Agreement, or other applicable participation, guaranty, or supplemental agreement. SBA Lenders further agree that a violation of Loan Program Requirements constitutes default under their respective agreements with SBA.

(1) *Additional agreements by CDCs.* By obtaining approval for 504 loans after October 20, 2017, a CDC consents to the remedies in § 120.1500(e)(3) and waives in advance any right it may have to contest the validity of the appointment of a receiver. The CDC agrees that its consent to SBA's application to a Federal court of competent jurisdiction for appointment of a receiver of SBA's choosing, an injunction or other equitable relief, and the CDC's consent in advance to the court's granting of SBA's application, may be enforced upon any basis in law or equity recognized by the court.

(2) *Additional agreements by SBA Supervised Lenders (except Other Regulated SBLCs).* By making SBA 7(a) guaranteed loans after October 20, 2017, an SBA Supervised Lender (except an Other Regulated SBLC) consents to the remedies in § 120.1500(c)(3) and waives in advance any right it may have to contest the validity of the appointment of a receiver. The SBA Supervised Lender agrees that its consent to SBA's application to a Federal court of competent jurisdiction for appointment of a receiver of SBA's choosing, an injunction or other equitable relief, and the SBA Supervised Lender's consent in advance

to the court's granting of SBA's application, may be enforced upon any basis in law or equity recognized by the court.

(b) *Scope.* SBA may undertake one or more of the enforcement actions listed in §120.1500 or as otherwise authorized by law, if SBA determines that the grounds applicable to the enforcement action exist. Paragraphs (c) through (e) of this section list the grounds that trigger enforcement actions against each type of SBA Lender. In general, the grounds listed in paragraph (c) apply to all SBA Lenders. However, certain enforcement actions against SBA Supervised Lenders require the existence of certain grounds, as set forth in paragraphs (d) and (e). In addition, paragraph (f) of this section lists two additional grounds for taking enforcement action against CDCs that do not apply to other SBA Lenders.

(c) *Grounds in general.* Except as provided in paragraphs (d) and (e) of this section, the grounds that may trigger an enforcement action against any SBA Lender (regardless of its Risk Rating) include:

(1) Failure to maintain eligibility requirements for specific SBA programs and delegated authorities, including but not limited to: 7(a), PLP, SBAExpress, 504, ALP, PCLP, the alternative loss reserve pilot program and any pilot loan program;

(2) Failure to comply materially with any requirement imposed by Loan Program Requirements;

(3) Making a material false statement or failure to disclose a material fact to SBA. (A material fact is any fact which is necessary to make a statement not misleading in light of the circumstances under which the statement was made.);

(4) Not performing underwriting, closing, disbursing, servicing, liquidation, litigation or other actions in a commercially reasonable and prudent manner for 7(a) or 504 loans, respectively, as applicable. Evidence of such performance or actions may include, but is not limited to, the SBA Lender having a repeated Less Than Acceptable Risk Rating (generally in conjunction with other evidence) or an on-site review/examination assessment which is Less Than Acceptable;

(5) Failure within the time period specified to correct an underwriting, closing, disbursing, servicing, liquidation, litigation, or reporting deficiency, or failure in any material respect to take other corrective action, after receiving notice from SBA of a deficiency and the need to take corrective action;

(6) Engaging in a pattern of uncooperative behavior or taking an action that SBA determines is detrimental to an SBA program, that undermines management or administration of a program, or that is not consistent with standards of good conduct. Prior to issuing a notice of a proposed enforcement action or immediate suspension under §120.1500 based upon this paragraph, SBA must send prior written notice to the SBA Lender explaining why the SBA Lender's actions were uncooperative, detrimental to the program, undermined SBA's management of the program, or were not consistent with standards of good conduct. The prior notice must also state that the SBA Lender's actions could give rise to a specified enforcement action, and provide the SBA Lender with a reasonable time to cure the deficiency before any further action is taken;

(7) Repeated failure to correct continuing deficiencies;

(8) Unauthorized disclosure of Reports, Risk Rating, or Confidential Information;

(9) Any other reason that SBA determines may increase SBA's financial risk (for example, repeated Less Than Acceptable Risk Ratings (generally in conjunction with other indicators of increased financial risk) or indictment on felony or fraud charges of an officer, key employee, or loan agent involved with SBA loans for the SBA Lender);

(10) As otherwise authorized by law; and

(11) For immediate suspension of all SBA Lenders from delegated authorities—upon a determination by SBA that one or more of the grounds in paragraph (c) or paragraph (f) of this section, as applicable, exist and that immediate action is needed to prevent significant impairment of the integrity of the 7(a) or 504 loan program.

(12) For immediate suspension of all SBA Lenders except SBA Supervised

Lenders from the authority to participate in the SBA loan program, including the authority to make, service, liquidate, or litigate 7(a) or 504 loans—upon a determination by SBA that one or more of the grounds in paragraph (c) or paragraph (f) of this section, as applicable, exist and that immediate action is needed to prevent significant impairment of the integrity of the 7(a) or 504 loan program.

(d) *Grounds required for certain enforcement actions against SBA Supervised Lenders (except Other Regulated SBLCs) or, as applicable, Other Persons.* For purposes of Subpart I, Other Person means a Management Official, attorney, accountant, appraiser, Lender Service Provider or other individual involved in the SBA Supervised Lender's operations. For the below listed SBA Supervised Lender enforcement actions, the grounds that are required to take the enforcement action are:

(1) *For SBA program suspensions and revocations*—

(i) False statements knowingly made in any required written submission to SBA; or

(ii) An omission of a material fact from any written submission required by SBA; or

(iii) A willful or repeated violation of the Small Business Act (the Act) or SBA regulations; or

(iv) A willful or repeated violation of any condition imposed by SBA with respect to any application, request, or agreement with SBA; or

(v) A violation of any cease and desist order of SBA.

(2) *For SBA program immediate suspension*—SBA may suspend an SBA Supervised Lender, effective immediately, if in addition to meeting the grounds set forth in paragraph (d)(1) of this section, the Administrator (or the Deputy Administrator, only if the Administrator is unavailable to take such action) finds extraordinary circumstances and takes such action in order to protect the financial or legal position of the United States.

(3) *For cease and desist orders*—

(i) A violation of the Act or SBA regulations, or

(ii) Where an SBA Supervised Lender or Other Person engages in or is about to engage in any acts or practices that will violate the Act or SBA's regulations.

(4) *For an emergency cease and desist order*—

(i) Where grounds for cease and desist order are met,

(ii) The Administrator (or the Deputy Administrator, only if the Administrator is unavailable to take such action) finds extraordinary circumstances, and

(iii) In order to protect the financial or legal position of the United States.

(5) *For transfer of Loan portfolio*—

(i) Where a court has appointed a receiver; or

(ii) The SBA Supervised Lender is either not in compliance with capital requirements or is insolvent. An SBA Supervised Lender is insolvent within the meaning of this provision when all of its capital, surplus, and undivided profits are absorbed in funding losses and the remaining assets are not sufficient to pay and discharge its contracts, debts, and other obligations as they come due.

(6) *For transfer of servicing activity*—

(i) Where grounds for transfer of Loan portfolio are met; or

(ii) Where the SBA Supervised Lender is otherwise operating in an unsafe and unsound condition.

(7) *For order to remove Management Official*—where, in the opinion of the Administrator or his/her delegatee, the Management Official—

(i) Willfully and knowingly committed a substantial violation of the Act, SBA regulation, a final cease and desist order, or any agreement by the Management Official or the SBA Supervised Lender under the Act or SBA regulations, or

(ii) Willfully and knowingly committed a substantial breach of a fiduciary duty of that person as a Management Official and the violation or breach of fiduciary duty is one involving personal dishonesty on the part of such Management Official, or

(iii) The Management Official is convicted of a felony involving dishonesty or breach of trust and the conviction is no longer subject to further judicial review (excludes writ of habeas corpus).

(8) *For order to suspend or prohibit participation of Management Official* (interim measure pending removal)—

where SBA is undertaking enforcement action of removal of a Management Official.

(9) *For order to suspend or prohibit participation of Management Official due to criminal charges*—where the Management Official is charged in any information, indictment or complaint authorized by a United States attorney with a felony involving dishonesty or breach of trust.

(e) *Grounds required for certain enforcement actions against SBLCs and Other Regulated SBLCs*—(1) *Capital directive*. If the AA/CA determines that an SBLC is capitally impaired or is otherwise being operated in an imprudent manner, the AA/CA may, in addition to any other action authorized by law, issue a directive to the SBLC to increase capital consistent with §120.1500(d)(1).

(2) *Civil action for termination*. If an SBLC violates the Act or SBA regulations, SBA may institute a civil action to terminate SBLC rights, privileges, and the franchise under §120.1500(d)(2).

(f) *Additional grounds specific to CDCs*. In addition to the grounds set forth in paragraphs (b) and (c) of this section, SBA may take enforcement action against a CDC for:

(1) Failure to receive SBA approval for at least four 504 loans during the last two consecutive fiscal years, or

(2) For PCLP CDCs, failure to establish or maintain a LLRF as required by the PCLP.

[73 FR 75521, Dec. 11, 2008, as amended at 82 FR 39505, Aug. 21, 2017]

§120.1425 Grounds for enforcement actions—Intermediaries participating in the Microloan Program and NTAPs.

(a) *Agreement*. By participating in the SBA Microloan or NTAP program, Intermediaries and NTAPs automatically agree to the terms, conditions, and remedies in this Part 120 as if fully set forth in their participation agreement and all other agreements jointly executed by the Intermediary or NTAP and SBA.

(b) *Scope*. SBA may undertake one or more of the enforcement actions listed in §120.1540, or as otherwise authorized by law, if SBA determines that any of the grounds listed in paragraphs (c) through (e) of this section exist.

(c) *Grounds in general*—For any Intermediary or NTAP, grounds that may trigger enforcement action against the Intermediary or NTAP (regardless of its Risk Rating) include:

(1) Violation of any laws, regulations, or policies of the program; or

(2) Failure to meet any one of the following performance standards:

(i) Coverage of the service territory assigned by SBA, including honoring SBA's determined boundaries of neighboring intermediaries and NTAPs;

(ii) Fulfill reporting requirements;

(iii) Manage program funds and matching funds in a satisfactory and financially sound manner;

(iv) Communicate and file reports within six months after beginning participation in program;

(v) Maintain a currency rate of 85% or more for the Intermediary's SBA Microloan portfolio (that is, loans that are no more than 30 days late in scheduled payments);

(vi) Maintain a default rate in the Intermediary's Microloan portfolio of 15% or less of the cumulative dollars loaned under the program;

(vii) Maintain a staff trained in Microloan program issues and requirements; or

(viii) Any other reason that SBA determines may increase SBA's financial or program risk (for example, repeated Less Than Acceptable Risk Ratings (generally in conjunction with other indicators of increased risk) or indictment on felony or fraud charges of an officer, key employee, or loan agent involved with SBA programs for the Intermediary or NTAP).

(d) *Additional grounds specific to Intermediaries*. In addition to the grounds set forth in paragraph (c) of this section, SBA may take enforcement action against an Intermediary for:

(1) Failure to satisfactorily provide in-house technical assistance to Microloan clients and prospective Microloan clients; or

(2) Failure to close and fund the required number of microloans per year under §120.716.

(e) *Additional grounds specific to NTAPs*. In addition to grounds set forth in paragraph (c) of this section, SBA

may take enforcement action against an NTAP for failure to show that, for every 30 clients for which the NTAP provided technical assistance, at least one client received a loan from the private sector.

[73 FR 75521, Dec. 11, 2008, as amended at 80 FR 34047, June 15, 2015]

§ 120.1500 Types of enforcement actions—SBA Lenders.

Upon a determination that the grounds set forth in § 120.1400 exist, SBA may undertake, in SBA's discretion, one or more of the following enforcement actions for each of the types of SBA Lenders listed. SBA will take such action in accordance with procedures set forth in § 120.1600. If enforcement action is taken under this section and the SBA Lender fails to implement required corrective action in any material respect within the required timeframe in response to the enforcement action, SBA may take further enforcement action, as authorized by law. SBA's decision to take an enforcement action will not, by itself, invalidate a guaranty previously provided by SBA.

(a) *Enforcement actions for all SBA Lenders*—(1) *Imposition of portfolio guaranty dollar limit.* SBA may limit the maximum dollar amount that SBA will guarantee on the SBA Lender's SBA loans or debentures.

(2) *Suspension or revocation of delegated authority.* SBA may suspend or revoke an SBA Lender's delegated authority (including, but not limited to, PLP, SBA Express, or PCLP delegated authorities).

(3) *Suspension or revocation from SBA program.* SBA may suspend or revoke an SBA Lender's authority to participate in the SBA loan program, including the authority to make, service, liquidate, or litigate 7(a) or 504 loans. Section 120.1400(d)(1) sets forth the grounds for SBA program suspension or revocation of an SBA Supervised Lender (except Other Regulated SBLCs). The grounds for SBA program suspension or revocation for all other SBA Lenders are set forth in § 120.1400(c) and, as applicable, paragraph (f) of § 120.1400.

(4) *Immediate suspension.* SBA may suspend, effective immediately, an SBA Lender's delegated authority or authority to participate in the SBA loan program, or the authority to make, service, liquidate, or litigate 7(a) or 504 loans. Section 120.1400(d)(2) sets forth the grounds for SBA program immediate suspension of an SBA Supervised Lender (except Other Regulated SBLCs). The grounds for SBA program immediate suspension for all other SBA Lenders and the grounds for immediate suspension of delegated authority for all SBA Lenders are set forth in § 120.1400(c)(11) and § 120.1400(c)(12).

(5) *Debarment.* In accordance with 2 CFR Parts 180 and 2700, SBA may take any necessary action to debar a Person, as defined in § 120.10, including but not limited to an officer, a director, a general partner, a manager, an employee, an agent or other participant in the affairs of an SBA Lender's SBA operations.

(6) *Other actions available under law.* SBA may take all other enforcement actions against SBA Lenders available under law.

(b) *Enforcement actions specific to 7(a) Lenders.* In addition to those enforcement actions applicable to all SBA Lenders, SBA may suspend or revoke a 7(a) Lender's authority to sell or purchase loans or certificates in the Secondary Market.

(c) *Enforcement actions specific to SBA Supervised Lenders and Other Persons (except Other Regulated SBLCs).* In addition to those enforcement actions listed in paragraphs (a) and (b) of this section, SBA may take any one or more of the following enforcement actions specific to SBA Supervised Lenders and as applicable, Other Persons:

(1) *Cease and desist order.* SBA may issue a cease and desist order against the SBA Supervised Lender or Other Person. The Cease and Desist order may either require the SBA Supervised Lender or the Other Person to take a specific action, or to refrain from a specific action. The Cease and Desist Order may be issued as effective immediately (or as a proposal for Order). SBA may include in the cease and desist order the suspension of authority to lend.

(2) *Remove Management Official.* SBA may issue an order to remove a Management Official from office. SBA may

suspend a Management Official from office or prohibit a Management Official from participating in management of the SBA Supervised Lender or in reviewing, approving, closing, servicing, liquidating or litigating any 7(a) loan, or any other activities of the SBA Supervised Lender while the removal proceeding is pending in order to protect an SBA Supervised Lender or the interests of SBA or the United States.

(3) *Initiate request for appointment of receiver and/or other relief.* The SBA may make application to any Federal court of competent jurisdiction for the court to take exclusive jurisdiction, without notice, of an SBA Supervised Lender, and SBA shall be entitled to the appointment of a receiver of SBA's choosing to hold, administer, operate, and/or liquidate the SBA Supervised Lender; and to such injunctive or other equitable relief as may be appropriate. Without limiting the foregoing and with SBA's written consent, the receiver may take possession of the portfolio of 7(a) loans and sell such loans to a third party, and/or take possession of servicing activities of 7(a) loans and sell such servicing rights to a third party.

(4) *Civil monetary penalties for report filing failure.* SBA may seek civil penalties, in accordance with §120.465, against an SBA Supervised Lender that fails to file any regular or special report by its due date as specified by regulation or SBA written directive.

(d) *Enforcement actions specific to SBLCs.* In addition to those supervisory actions listed in paragraphs (a), (b), and (c) of this section, SBA may take the following enforcement actions specific to SBLCs.

(1) *Capital directive.* The AA/CA may issue a capital directive upon a determination that the grounds in §120.1400(e)(1) exist. A directive may order the SBLC to:

(i) Achieve its minimum capital requirement applicable to it by a specified date;

(ii) Adhere to a previously submitted capital restoration plan (provided under §120.462 or §120.1055) to achieve the applicable capital requirement;

(iii) Submit and adhere to a capital restoration plan acceptable to SBA describing the means and time schedule by which the SBLC will achieve the applicable capital requirement (The SBLC must provide its capital restoration plan within 30 days from the date of the SBA order unless SBA notifies the SBLC that the plan is to be filed within a different time period. SBA may perform an on-site examination (generally within 90 days after the restoration plan is submitted) to verify the implementation of the plan and verify that the SBLC meets minimum capital requirements.);

(iv) Refrain from taking certain actions without obtaining SBA's prior written approval (Such actions may include but are not limited to: paying any dividend; retiring any equity; maintaining a rate of growth that causes further deterioration in the capital percentage; securitizing any unguaranteed portion of its 7(a) loans; or selling participations in any of its 7(a) loans); or

(v) Undertake a combination of any of these or similar actions.

(2) *Civil action for termination.* SBA may institute a civil action to terminate the rights, privileges, and franchises of an SBLC.

(e) *Enforcement actions specific to CDCs.* In addition to those enforcement actions listed in paragraph (a) of this section, SBA may take any one or more of the following enforcement actions specific to CDCs:

(1) Require the CDC to transfer part or all of its existing 504 loan portfolio and/or part or all of its pending 504 loan applications to SBA, another CDC, or any other entity designated by SBA. Any such transfer may be on a temporary or permanent basis, in SBA's discretion; or

(2) Instruct the Central Servicing Agent to withhold payment of servicing, late and/or other fee(s) to the CDC.

(3) Apply to any Federal court of competent jurisdiction for the court to take exclusive jurisdiction, without notice, of the CDC, and SBA shall be entitled to the appointment of a receiver of SBA's choosing to hold, administer, operate and/or liquidate the CDC; and to such injunctive or other equitable relief as may be appropriate. Without limiting the foregoing and with SBA's

consent, the receiver may take possession of the portfolio of 504 loans and/or pending 504 loan applications, including for the purpose of carrying out an enforcement order under paragraph (e)(1) of this section.

[73 FR 75521, Dec. 11, 2008, as amended at 82 FR 39506, Aug. 21, 2017; 84 FR 12061, Apr. 1, 2019]

§ 120.1510 Other Regulated SBLCs.

Other Regulated SBLCs are exempt from §§ 120.465, 120.1050(b), 120.1400(d), 120.1500(c), and 120.1600(b). This exemption is not intended to preclude SBA from seeking any other remedy authorized by law or equity.

[73 FR 75521, Dec. 11, 2008]

§ 120.1511 Certification and other reporting and notification requirements for Other Regulated SBLCs.

(a) *Certification*. An SBLC seeking Other Regulated SBLC status must certify to SBA in writing that its lending activities are subject to regulation by a Federal Financial Institution Regulator or state banking regulator. This certification must be executed by the chair of the board of directors of the SBLC and submitted to SBA either:

(1) Within 60 calendar days of the effective date of this section or

(2) If the SBLC becomes subject to regulation by a Federal Financial Institution Regulator or state banking regulator after the effective date of this section for any reason (e.g. license transfers), within 60 days of the date that the SBLC becomes directly examined and directly regulated by such regulator.

(b) *Contents of Certification:* This certification must include:

(1) The identity of the Federal Financial Institution Regulator or state banking regulator that regulates the lending activities of the SBLC;

(2) A statement that the Federal Financial Institution Regulator or state banking regulator identified in paragraph (b)(1) of this section regularly conducts safety and soundness examinations on the SBLC itself and not only on the SBLC's parent company or affiliate, if any; and

(3) The date of the most recent safety and soundness examination conducted on the SBLC by the Federal Financial Institution Regulator or state banking regulator. To qualify as an Other Regulated SBLC, the SBLC must have received this examination within the past 3 years of the date of certification.

(c) *Notification of examination*. An Other Regulated SBLC must notify SBA in writing each time a Federal Financial Institution Regulator or state banking regulator conducts a safety and soundness examination, and this notification must be submitted to SBA within 30 calendar days of the SBLC receiving the results of the examination. To retain its status as an Other Regulated SBLC, the Other Regulated SBLC must receive such examination, and provide the written notification to SBA, at least once every two years following initial certification.

(d) *Report*. An Other Regulated SBLC must report in writing to SBA on its interactions with other Federal Financial Institution Regulators or state banking regulator (e.g., the results of the safety and soundness examinations and any order issued against the Other Regulated SBLC), to the extent allowed by law.

(e) *Notification of change in status*. If, for any reason, an Other Regulated SBLC becomes no longer subject to regulation by a Federal Financial Institution Regulator or state banking regulator, the Other Regulated SBLC must immediately notify SBA in writing, and the exemption provided in § 120.1510 will immediately no longer apply.

(f) *Extension of timeframes*. SBA may in its discretion extend any timeframe imposed on the SBLC under this section if the SBLC can show good cause for any delay in meeting the time requirement. The SBLC may appeal this decision to the AA/CA.

(g) *Failure to satisfy requirements*. In the event that an SBLC fails to satisfy the requirements set forth in paragraphs (a), (b), and (c) of this section, then the exemption provided in § 120.1510 will not apply to the SBLC.

[73 FR 75521, Dec. 11, 2008]

§ 120.1540 Types of enforcement actions—Intermediaries participating in the Microloan Program and NTAPs.

Upon a determination that any ground set out in § 120.1425 exists, the SBA may take in its discretion, one or more of the following enforcement actions against an Intermediary or NTAP:

(a) Suspension or pre-revocation sanctions which may include, but are not limited to:

(1) Accelerated reporting requirements;

(2) Accelerated loan repayment requirements for outstanding program debt to SBA, as applicable;

(3) Imposition of a temporary lending moratorium, as applicable; or

(4) Imposition of a temporary training moratorium.

(b) Revocation of authority to participate in the Microloan program which will include:

(1) Removal from the program;

(2) Liquidation of Intermediary's Microloan Revolving Fund and Loan Loss Reserve Fund accounts by SBA, and application of the liquidated funds to any outstanding balance owed to SBA;

(3) Payment of outstanding debt to SBA by the Intermediary;

(4) Forfeiture or repayment of any unused grant funds by the Intermediary or NTAP;

(5) Debarment of the organization from receipt of federal funds until loan and grant repayments are met; or

(6) Taking such other actions available under law.

[73 FR 75521, Dec. 11, 2008]

§ 120.1600 General procedures for enforcement actions against SBA Lenders, SBA Supervised Lenders, Other Regulated SBLCs, Management Officials, Other Persons, Intermediaries, and NTAPs.

(a) *In general.* Except as otherwise set forth for the enforcement actions listed in paragraphs (a)(6), (b) and (c) of this section, SBA will follow the procedures listed below.

(1) *SBA's notice of enforcement action.* (i) When undertaking an immediate suspension under § 120.1500(a)(4), or prior to undertaking an enforcement action set forth in § 120.1500(a), (b), and (e) and § 120.1540, SBA will issue a written notice to the affected SBA Lender, Intermediary, or NTAP identifying the proposed enforcement action or notifying it of an immediate suspension. The notice will set forth in reasonable detail the underlying facts and reasons for the proposed action or immediate suspension. If the notice is for a proposed or immediate suspension, SBA will also state the scope and term of the proposed or immediate suspension.

(ii) If a proposed enforcement action or immediate suspension is based upon information obtained from a third party other than the SBA Lender, Intermediary, NTAP or SBA, SBA's notice of proposed action or immediate suspension will provide copies of documentation received from such third party, or the name of the third party in case of oral information, unless SBA determines that there are compelling reasons not to provide such information. If compelling reasons exist, SBA will provide a summary of the information it received to the SBA Lender, Intermediary, or NTAP.

(2) *SBA Lender, Intermediary, or NTAP's opportunity to object.* (i) An SBA Lender, Intermediary, or NTAP that desires to contest a proposed enforcement action or an immediate suspension must file, within 30 calendar days of its receipt of the notice or within some other term established by SBA in its notice, a written objection with the appropriate Office of Capital Access official in accordance with Delegations of Authority or other SBA official identified in the notice. Notice will be presumed to have been received within five days of the date of the notice unless the SBA Lender, Intermediary, or NTAP can provide compelling evidence to the contrary.

(ii) The objection must set forth in detail all grounds known to the SBA Lender, Intermediary, or NTAP to contest the proposed action or immediate suspension and all mitigating factors, and must include documentation that the SBA Lender, Intermediary, or NTAP believes is most supportive of its objection. An SBA Lender, Intermediary, or NTAP must exhaust this

administrative remedy in order to preserve its objection to a proposed enforcement action or an immediate suspension.

(iii) If an SBA Lender, Intermediary, or NTAP can show legitimate reasons as determined by SBA in SBA's discretion why it does not understand the reasons given by SBA in its notice of the action, the Agency will provide clarification. SBA will provide the requested clarification in writing to the SBA Lender, Intermediary, or NTAP or notify the SBA Lender, Intermediary, or NTAP in writing that SBA has determined that such clarification is not necessary. SBA, in its discretion, will further advise in writing whether the SBA Lender, Intermediary, or NTAP may have additional time to present its objection to the notice. Requests for clarification must be made to the appropriate Office of Capital Access official in accordance with Delegations of Authority in writing and received by SBA within the 30 day timeframe or the timeframe given by the notice for response.

(iv) An SBA Lender, Intermediary, or NTAP may request additional time to respond to SBA's notice if it can show that there are compelling reasons why it is not able to respond within the 30 day timeframe or the response timeframe given by the notice. If such requests are submitted to the Agency, SBA may, in its discretion, provide the SBA Lender, Intermediary, or NTAP with additional time to respond to the notice of proposed action or immediate suspension. Requests for additional time to respond must be made in writing to the appropriate Office of Capital Access official in accordance with Delegations of Authority or other official identified in the notice and received by SBA within the 30 day timeframe or the response timeframe given by the notice.

(v) Prior to the issuance of a final decision by SBA, if an SBA Lender, Intermediary, or NTAP can show that there is newly discovered material evidence which, despite the SBA Lender, Intermediary, or NTAP's exercise of due diligence, could not have been discovered within the timeframe given by SBA to respond to a notice, or that there are compelling reasons beyond the SBA Lender, Intermediary, or NTAP's control as to why it was not able to present a material fact or argument to SBA, and that the SBA Lender, Intermediary, or NTAP has been prejudiced by not being able to present such information, the SBA Lender, Intermediary, or NTAP may submit such information to SBA and request that the Agency consider such information in its final decision.

(3) *SBA's notice of final agency decision where SBA Lender, Intermediary, or NTAP filed objection to the proposed action or immediate suspension.* (i) If the affected SBA Lender, Intermediary, or NTAP files a timely written objection to a proposed enforcement action other than an immediate suspension in accordance with this section, SBA must issue a written notice of final decision to the affected SBA Lender, Intermediary, or NTAP advising whether SBA is undertaking the proposed enforcement action and setting forth the grounds for the decision. SBA will issue such a notice of decision within 90 days of either receiving the objection or from when additional information is provided under paragraph (a)(2)(v) or (a)(3)(iii) of this section, whichever is later, unless SBA provides notice that it requires additional time.

(ii) If the affected SBA Lender, Intermediary, or NTAP files a timely written objection to a notice of immediate suspension, SBA must issue a written notice of final decision to the affected SBA Lender, Intermediary, or NTAP within 30 days of receiving the objection advising whether SBA is continuing with the immediate suspension, unless SBA provides notice that it requires additional time. If the SBA Lender, Intermediary, or NTAP submits additional information to SBA (under paragraph (a)(2)(v) or (a)(3)(iii) of this section) after submitting its objection but before SBA issues its final decision, SBA must issue its final decision within 30 days of receiving such information, unless SBA provides notice that it requires additional time.

(iii) Prior to issuing a notice of decision, SBA in its discretion can request additional information from the affected SBA Lender, Intermediary, NTAP or other parties and conduct any

other investigation it deems appropriate. If SBA determines, in its discretion, to consider an untimely objection, it must issue a notice of final decision pursuant to this paragraph (a)(3).

(4) *SBA's notice of final agency decision where no filed objection or untimely objection not considered.* If SBA chooses not to consider an untimely objection or if the affected SBA Lender, Intermediary, or NTAP fails to file a written objection to a proposed enforcement action or an immediate suspension, and if SBA continues to believe that such proposed enforcement action or immediate suspension is appropriate, SBA must issue a written notice of final decision to the affected SBA Lender, Intermediary, or NTAP that SBA is undertaking one or more of the proposed enforcement actions against the SBA Lender, Intermediary, or NTAP or that an immediate suspension of the SBA Lender, Intermediary, or NTAP will continue. Such a notice of final decision need not state any grounds for the action other than to reference the SBA Lender, Intermediary, or NTAP's failure to file a timely objection, and represents the final agency decision.

(5) *Appeals.* An SBA Lender, Intermediary, or NTAP may appeal the final agency decision only in the appropriate federal district court.

(6) *Receiverships of Certified Development Companies and/or other relief.* If SBA undertakes the appointment of a receiver for a Certified Development Company and/or injunctive or other equitable relief, paragraphs (a)(1) through (5) of this section will not apply and SBA will follow the applicable procedures under Federal law to obtain such remedies and to enforce the Certified Development Company's consent and waiver in advance to those remedies.

(b) *Procedures for certain enforcement actions against SBA Supervised Lenders (except Other Regulated SBLCs) and, where applicable, Management Officials and Other Persons*—(1) *Suspension and revocation actions and cease and desist orders.* If SBA seeks to suspend or revoke loan program authority (including, the authority to make, service, liquidate, or litigate SBA loans), or issue a cease and desist order to an SBA Supervised Lender or, as applicable, Other Person, SBA will follow the procedures below in lieu of those in paragraph (a) of this section.

(i) *Show cause order and hearing.* The Administrator will serve upon the SBA Supervised Lender or Other Person an order to show cause why an order suspending or revoking the authority or why a cease and desist order should not be issued. The show cause order will contain a statement of the matters of fact and law asserted by SBA, as well as the legal authority and jurisdiction under which an administrative hearing will be held, and will set forth the place and time of the administrative hearing. The hearing will be conducted by an administrative law judge in accordance with 5 U.S.C. 554–557, 15 U.S.C. 650, and applicable sections of part 134 of this chapter. The Administrative Law Judge will issue a recommended decision based on the record.

(ii) *Witnesses.* The party calling witnesses will pay the witness the same fees and mileage paid witnesses for their appearance in U.S. courts.

(iii) *Administrator finding and order issuance.* If after the administrative hearing, or the SBA Supervised Lender's or Other Person's waiver of the administrative hearing, the Administrator determines that the order should be issued, the Administrator will issue an order to suspend or revoke authority or a cease and desist order, as applicable. The order will include a statement of findings, the grounds and reasons, and will specify the order's effective date. SBA will serve the order on the SBA Supervised Lender or Other Person. The Administrator may delegate the power to issue a cease and desist order or to suspend or revoke loan program authority only if the Administrator is unavailable and only to the Deputy Administrator.

(iv) *Judicial review.* The order constitutes a final agency action. The SBA Supervised Lender or Other Person will have 20 days from the order issuance date to file an appeal in the appropriate federal district court.

(2) *Immediate suspension or immediate cease and desist order.* If SBA undertakes an immediate suspension of authority to participate in the 7(a) loan program or immediate cease and desist

order against an SBA Supervised Lender or, as applicable, Other Person, SBA will within two business days follow the procedures set forth in paragraph (b)(1) of this section.

(3) *Removal of Management Official.* If SBA undertakes the removal of a Management Official of an SBA Supervised Lender, SBA will follow the procedures below in lieu of those in paragraph (a) of this section.

(i) *Notice and hearing.* SBA will serve upon the Management Official and the SBA Supervised Lender written notice of intention to remove that includes a statement of the facts constituting the grounds and the date, time, and place for an administrative hearing. The administrative hearing will be held between 30 and 60 days from the date notice is served, unless an earlier or later date is set at the request of the Management Official for good cause shown or at the request of the Attorney General. The hearing will be conducted in accordance with 5 U.S.C. 554–557, 15 U.S.C. 650 and applicable sections of part 134 of this chapter. Failure of the Management Official to appear at the administrative hearing will constitute consent to the removal order. SBA will serve on the SBA Supervised Lender a copy of each notice that is served on a Management Official.

(ii) *Suspension from office or prohibition in participation, pending removal.* The suspension or prohibition will take effect upon service of intention to remove the Management Official or such subsequent time as the Administrator or his/her delegate deems appropriate and serves notice. It will remain in effect pending the completion of the administrative proceedings to remove and until such time as either SBA dismisses the charges in the removal notice or, if an order to remove or prohibit participation is issued, until the effective date of an order to remove or prohibit. In the case of suspension or prohibition following criminal charges, it may remain in effect until the information, indictment, or complaint is finally disposed of, or until the suspension is terminated by SBA or by order of a district court. A Management Official may appeal to the appropriate federal district court for a stay of the suspension or prohibition pending completion of the administrative hearing not later than 10 days from the suspension or prohibition's effective date.

(iii) *Decision.* SBA may issue the order of removal if the Management Official consents or is convicted of the criminal charges and the judgment is not subject to further judicial review (not including writ of habeas corpus), or if upon a record of a hearing, SBA finds that any of the notice grounds have been established. After the hearing, in the latter case, and within 30 days after SBA has notified the parties that the case has been submitted for final decision, SBA will render a decision (which includes findings of fact upon which the decision is predicated) and issue and serve an order upon each party to the proceeding. The decision will constitute final agency action.

(iv) *Effective date and judicial review.* The removal order will take effect 30 days after date of service upon the SBA Supervised Lender and the Management Official except in case of consent which will be effective at the time specified in the order or in case of removal for conviction on criminal charges the order will be effective upon removal order service on the SBA Supervised Lender and the Management Official. The order will remain effective and enforceable, except to the extent it is stayed, modified, terminated, or set aside by Administrator or a reviewing court. The adversely affected party will have 20 days from the order issuance date to seek judicial review in the appropriate federal district court.

(4) *Receiverships, transfer of assets and servicing activities.* If SBA undertakes the appointment of a receiver for, or the transfer of assets or servicing rights of an SBA Supervised Lender and/or injunctive or other equitable relief, SBA will follow the applicable procedures under Federal law to obtain such remedies and to enforce the SBA Supervised Lender's consent and waiver in advance to those remedies.

(5) *Civil penalties for report filing failure.* If SBA seeks to impose civil penalties against an SBA Supervised Lender for failure to file a report in accordance with SBA regulations or written directive, SBA will follow the procedures set forth for enforcement actions in § 120.465.

(c) *Additional procedures for certain enforcement actions against SBLCs. Capital directive*—(1) *Notice of intent to issue capital directive.* SBA will notify an SBLC in writing of its intention to issue a directive. The notice will state:

(i) Reasons for issuance of the directive and

(ii) The proposed contents of the directive.

(2) *Response to notice.* (i) An SBLC may respond to the notice by stating why a capital directive should not be issued and/or by proposing alternative contents for the capital directive or seeking other appropriate relief. The response must include any information, mitigating circumstances, documentation, or other relevant evidence that supports its position. The response may include a plan for achieving the minimum capital requirement applicable to the SBLC. The response must be in writing and delivered to the SBA within 30 days after the date on which the SBLC received the notice. In its discretion, SBA may extend the time period for good cause. SBA may shorten the 30-day time period:

(A) When, in the opinion of SBA, the condition of the SBLC so requires, provided that the SBLC will be informed promptly of the new time period;

(B) With the consent of the SBLC; or

(C) When the SBLC already has advised SBA that it cannot or will not achieve its applicable minimum capital requirement.

(ii) Failure to respond within 30 days or such other time period as may be specified by SBA will constitute a waiver of any objections to the proposed capital directive.

(3) *Decision.* After the closing date of the SBLC's response period, or receipt of the SBLC's response, if earlier, SBA may seek additional information or clarification of the response. Thereafter, SBA will determine whether or not to issue a capital directive, and if one is to be issued, whether it should be as originally proposed or in modified form.

(4) *Issuance of a capital directive.* (i) A capital directive will be served by delivery to the SBLC. It will include, or be accompanied by, a statement of reasons for its issuance.

(ii) A capital directive is effective immediately upon its receipt by the SBLC, or upon such later date as may be specified therein, and will remain effective and enforceable until it is stayed, modified, or terminated by SBA.

(5) *Reconsideration based on change in circumstances.* Upon a change in circumstances, an SBLC may request SBA to reconsider the terms of its capital directive or may propose changes in the plan to achieve the SBLC's applicable minimum capital requirement. SBA also may take such action on its own initiative. SBA may decline to consider requests or proposals that are not based on a significant change in circumstances or are repetitive or frivolous. Pending a decision on reconsideration, the capital directive and plan will continue in full force and effect.

(6) *Relation to other administrative actions.* A capital directive may be issued in addition to, or in lieu of, any other action authorized by law, including cease and desist proceedings. SBA also may, in its discretion, take any action authorized by law, in lieu of a capital directive, in response to an SBLC's failure to achieve or maintain the applicable minimum capital requirement.

(7) *Appeals.* The capital directive constitutes a final agency action. An SBLC may appeal the final agency decision only in the appropriate federal district court.

[73 FR 75521, Dec. 11, 2008, as amended at 82 FR 39506, Aug. 21, 2017]

Subpart J—Establishment of SBA Secondary Market Guarantee Program for First Lien Position 504 Loan Pools

SOURCE: 74 FR 56093, Oct. 30, 2009, unless otherwise noted.

§ 120.1700 Definitions used in subpart J.

504 financing. The loans made to a small business to fund a Project under the SBA's development company loan program authorized by Title V of the Small Business Investment Act of 1958.

Affiliate. A person or entity SBA determines to be an affiliate of a Program Participant pursuant to the application of the principles and guidelines set forth in § 121.103 of this Title.

Central Servicing Agent or CSA. The entity serving as SBA's central servicing agent for the Program.

Certified Development Company or CDC. An entity that meets the definition of a Certified Development Company as defined in § 120.10 of this Part.

Current. That no scheduled payment owed by an Obligor pursuant to a Pool Note is over 29 days past due.

First Lien Position 504 Loan. The financing provided by the First Lien Position 504 lender that is part of the 504 project financing.

First Lien Position 504 Loan Pool Guarantee Agreement. The agreement, in the form approved by SBA, wherein entities agree to participate in the forming of a Pool under the Program, available at *http://www.sba.gov/aboutsba/sbaprograms/elending/index.html/*.

Guide. The First Lien Position 504 Loan Pooling Program Guide published by SBA which provides information applicable to the Program including, among other things, requirements relating to the formation of a Pool, available at *http://www.sba.gov/aboutsba/sbaprograms/elending/index.html/*.

Liquidation Proceeds. Cash, including insurance proceeds, proceeds of any foreclosed-on property disposition, revenues received with respect to the conservation and disposition of a foreclosed-on property or repossessed collateral, including any real property securing the Pool Loan, consisting of a commercial property or residential property and any improvements thereon, and any other amounts received in connection with the liquidation of the Pool Loan, whether through Seller's sale, foreclosure sale, any offset or workout, or otherwise.

Loan Interest. The right to receive the owned portion of the principal balance of the Pool Loan together with interest thereon at a per annum rate in effect from time to time in accordance with the First Lien Position 504 Loan Pool Guarantee Agreement.

Maturity. The maturity of the Loan Interest in the Pool that has the longest remaining term of any Loan Interest in the Pool. The maturity will change from time to time due to prepayment or default on Loan Interests in the Pool.

Ongoing Guarantee Fee. An annual fee collected monthly and based on the percentage of the Pool Loan amount, pursuant to section 503(C)(3)(B)(ii) of the Recovery Act, to result in a cost of the loan guarantee of zero as determined under the Federal Credit Reform Act of 1990, as amended. The funds generated by the fee serve as a reserve to pay for program losses.

Obligor. The obligor(s) under a Pool Note.

Pool. The aggregate of Loan Interests formed into a single pool by the Pool Originator in accordance with the Program. The Pool is comprised of an unguaranteed portion and an SBA-guaranteed portion. The unguaranteed portion of the Pool backs the Pool Originator Receipt, and cannot be sold to Pool Investors. The SBA-guaranteed portion of the Pool backs the Pool Certificates sold to Pool Investors. The Seller's Loan Interest is not included in the Pool.

Pool Assembler. An entity that meets the qualifications of a Pool Assembler as set forth in section 120.630 of this Part and has been approved as such by SBA.

Pool Certificate. The document representing a beneficial fractional interest in the SBA-guaranteed portion of a Pool.

Pooled. When one or more Loan Interests in a Pool Loan has been put into a Pool.

Pooling. The transfer of one or more Loan Interests in a Pool Loan into a Pool.

Pool Investor. An entity which holds a Pool Certificate in accordance with Program Rules and Regulations.

Pool Loan. A loan that meets the Program eligibility requirements as set forth in § 120.1704 of this subpart J and has been pooled.

Pool Loan Receivables. Pool Loan payments, prepayments, or collections made in connection with the Pool Loan by the Obligor pursuant to Pool Note or any other Pool Loan documents or agreements, or by another person or entity made on behalf of any such Pool

Loan obligor, and Liquidation Proceeds.

Pool Note. The document evidencing a Pool Loan.

Pool Originator. An entity approved by SBA to pool Loan Interests under the Program.

Pool Originator Receipt. The document evidencing the Pool Originator's retained ownership in a Pool it has formed under the Program.

Premier Certified Lenders Program. The program defined in §120.845 of this Part.

Program. The program authorized by section 503 of the American Recovery and Reinvestment Act of 2009.

Program Participant. An entity that executes the First Lien Position 504 Loan Pool Guarantee Agreement as Seller, Pool Originator, or Pool Investor, and any successors or assignees thereof.

Program Participant Associate. (1) An officer, director, key employee, or holder of 20 percent or more of the value of a Program Participant's stock or debt instruments, or (2) Any individual in which one or more individuals referred to in paragraph (1) of this definition, or a spouse, or child, or sibling, or the spouse of any such individual, owns or controls at least 20 percent.

Program Preference. Any arrangement giving the Seller, Pool Originator, or a Program Associate or Affiliate of Seller or Pool Originator, a preference or benefit of proportion greater than its Loan Interest as compared to Pool Originator, Pool Investor, or SBA relating to the making, servicing, or liquidation of the Loan with respect to such things as repayment, collateral, guarantees, control, maintenance of a compensating balance, purchase of a certificate of deposit or acceptance of a separate or companion loan, without SBA's consent. Seller's agreement to grant a Pool Loan's Obligor a deferment in return for receiving more collateral on a different loan owned by Seller is an example of a preference.

Program Rules and Regulations. This subpart J, as may be amended from time to time by SBA (the Program Regulations), the First Lien Position 504 Loan Pool Guarantee Agreement, any other Program agreements signed by a Program Participant, if applicable, the Guide, the Recovery Act, and the provisions of subpart H governing Third Party Loans and Third Party Lenders.

Project. A project as defined by §120.802 of the Part.

SBA. The United States Small Business Administration, an agency of the United States Government.

Seller. An entity that has sold a Pool Loan to a Pool Originator to be Pooled and any successor entity that has executed the First Lien Position 504 Loan Pool Guaranty Agreement pursuant to §120.1707.

Seller's Pool Loan. The Pool Loan sold to a Pool Originator pursuant to the First Lien Position 504 Loan Pool Guarantee Agreement.

Seller Receipt. The document that evidences a Seller's Loan Interest.

Servicing Retention Amount. The amount of a Pool Loan interest payment retained by Seller for servicing the Pool Loan that is payable and calculated pursuant to the First Lien Position 504 Loan Pool Guarantee Agreement.

Weighted Average Interest Rate. The dollar-weighted average interest rate of a Pool Certificate calculated by multiplying the interest rate of each Loan Interest in the Pool by the ratio of that Loan Interest's current outstanding principal in the SBA-guaranteed portion of the Pool (that is, the portion of the Pool Loan backing the Pool Certificates) to the current aggregate or outstanding principal of each Loan Interest in the SBA-guaranteed portion of the Pool, and adding the sum of the resulting products. The Pool Certificate interest rate will fluctuate over the life of the Pool as defaults, prepayments and normal repayments applicable to Loan Interests in the Pool occur.

Weighted Average Maturity. The weighted average maturity of a Pool Certificate is a dollar weighted average maturity that is calculated by multiplying the remaining term, in months, of each Loan Interest in a Pool by the ratio of that Loan Interest's current outstanding pooled principal to the current aggregate outstanding pooled principal of all Loan Interests in the Pool, and adding the sum of the resulting products. The weighted average

maturity of a Pool Certificate will fluctuate over the life of the Pool as Loan Interest defaults, prepayments and normal Loan Interest repayments occur.

§ 120.1701 Program purpose.

As authorized by the American Recovery and Reinvestment Act of 2009 (Recovery Act), SBA establishes the Program to authorize an entity to apply for SBA's guarantee of Pools comprised of portions of First Lien Position 504 Loans backing Pool Certificates to be sold to Pool Investors. The purpose of the Program is to temporarily provide a federal guarantee for Pools of First Lien Position 504 Loans to facilitate the sale of such loans and increase the liquidity of the lenders holding the loans so that the lenders can use the sale proceeds to fund more such loans. The Program's authorization expires on September 23, 2012 and the Administrator may guarantee not more than $3,000,000,000 of pools under this authority pursuant to section 503(c)(B)(iii) of the Recovery Act, as amended by section 1119 of the Small Business Jobs Act of 2010.

[61 FR 3235, Jan. 31, 1996, as amended at 76 FR 63547, Oct. 12, 2011]

§ 120.1702 Program fee.

Ongoing Guarantee Fee. The Ongoing Guarantee Fee is payable to SBA, and it is calculated and payable monthly from the amounts received in respect of interest on Loan Interests in the SBA-guaranteed portion of a Pool. This amount is set forth in the First Lien Position 504 Loan Pool Guarantee Agreement. This fee is used to pay program losses.

§ 120.1703 Qualifications to be a Pool Originator.

(a) *Application to become Pool Originator.* The application to become a Pool Originator is available from the SBA and can be found on SBA's website. In order to qualify as a Pool Originator, an entity must send the application to the SBA and certify that it is a Pool Assembler or it:

(1) Is regulated by the appropriate agency as defined in section 3(a)(34)(G) of the Securities Exchange Act of 1934 (15 U.S.C. 78c(a)(34)(G));

(2) Meets all financial and other applicable requirements of its regulatory authority and the Government Securities Act of 1986, as amended (Pub. L. 99–571, 100 Stat. 3208);

(3) Has the financial capability to originate acceptable pools consisting of eligible First Lien Position 504 Loans in sufficient quantity to support the issuance of Pool Certificates;

(4) Is in good standing with SBA (as the SBA determines), and is Satisfactory with the Office of the Comptroller of the Currency (OCC) if it is a national bank, the Federal Deposit Insurance Corporation if it is a bank not regulated by the OCC, the Financial Institutions Regulatory Authority if it is a member, the National Credit Union Administration if it is a credit union, as determined by SBA; and

(5) for any Pool Originator that is an SBA Lender, that the SBA Lender has satisfactory SBA performance, as determined by SBA in its sole discretion.

(b) *Approval by SBA.* An entity may not submit applications to form Pools to the CSA until SBA has approved its application to become a Pool Originator.

(c) *Conduct of business by Pool Originator.* An entity continues to qualify as a Pool Originator so long as it:

(1) Meets the eligibility standards in paragraph (a) of this section;

(2) Conducts its business in accordance with SBA regulations and accepted securities or banking industry practices, ethics, and standards;

(3) Maintains its books and records in accordance with generally accepted accounting principles or in accordance with the guidelines of the regulatory body governing its activities; and

(4) Has not been suspended or terminated from the Program by SBA.

[74 FR 56093, Oct. 30, 2009, as amended at 82 FR 39506, Aug. 21, 2017]

§ 120.1704 Pool Loans eligible for Pooling.

(a) *General Pool Loan eligibility requirements.* For a First Lien Position 504 Loan to be eligible for Pooling it must:

(1) Be a loan that is:

(i) A Third Party Loan as defined in § 120.801(c)(3);

(ii) Made by a private sector lender acceptable to SBA in its sole discretion; and

(iii) Secured by a first lien on the Project Property as defined in §120.801 of this chapter;

(2) Be part of a 504 financing that is comprised of only one Third Party Loan and one CDC 504 loan; the CDC 504 loan must be funded by a Debenture that was been sold on or after February 17, 2009;

(3) Be Current and have been Current for the six-month-period immediately prior to the date the Pool is formed or for the life of the Pool Loan, whichever time period is shorter;

(4) Have been made and closed in a commercially reasonable manner, consistent with prudent lending standards;

(5) Be part of a completed 504 financing, funded by a 504 debenture, which means that the Pool Loan must be fully disbursed and the debenture funding the related loan by a CDC must have been sold on or after February 17, 2009; and

(6) Not be:

(i) To a business deriving more than one-third of its gross annual revenue from legal gambling activities;

(ii) To a casino, gambling establishment, or casino hotel;

(iii) For financing the acquisition, construction or renovation of an aquarium, zoo, golf course, or swimming pool; or

(iv) To a business covered by a six-digit North American Industry Classification System (NAICS) code for casinos—713210 (''Casinos (Except Casino Hotels)''); casino hotels—721120 (''Casino Hotels''); other gambling institutions—713290 (''Other Gambling Industries''); golf courses—713910 (''Golf Courses and Country Clubs''); or aquariums and zoos—712130 (''Zoos and Botanical Gardens'').

(b) *SBA review of a Pool Loan prior to pool formation.* SBA has the right to review any Pool Loan before a Loan Interest in it is added to a Pool, and SBA may prohibit the Pool's formation as proposed based on SBA's review in SBA's sole discretion. In the event SBA decides to review Pool Loan documents related to a Loan Interest prior to the requested Pool formation, that Loan Interest may not be added to the Pool until SBA reviews and approves the Pool Loan for such purpose. Copies of Pool Loan documents related to underwriting and origination, and any other Pool Loan-related documents SBA may, in its sole discretion, request to review in writing, must be sent to SBA's Sacramento Pool Loan Processing Center. The Pool Originator must identify and SBA must review Pool Loan documents before a Loan Interest is added to a Pool if:

(1) The Pool Loan is to a business within NAICS code 713940 covering Fitness and Recreational Sports Centers; (If SBA determines that a Pool Loan has had any of its proceeds used for any of the restricted purposes listed above, the Pool Loan will be prohibited from being part of a Pool.)

(2) The Pool Loan was part of a 504 financing involving a 504 loan that was processed under SBA's Premier Certified Lenders Program; or

(3) The Project the Pool Loan financed included the refinancing of existing debt owed to the Seller or Third Party Lender (not including interim financing associated with the Project).

§120.1705 Pool formation requirements.

(a) *Initiation of Pool formation.* Only an entity approved by SBA to be a Pool Originator under the Program that continues to qualify to be a Pool Originator pursuant to this subpart may initiate the formation of a Pool. The Pool Originator creates the Pool subject to Program Rules and Regulations, including the parameters set forth in the Guide, and SBA approval.

(b) *Adjustment of Pool requirements.* SBA may adjust the Pool characteristics periodically based on program experience and market conditions and will publish a revised version of the Guide in the FEDERAL REGISTER to implement such adjustments. Any such adjustments shall not affect Pools formed prior to the adjustment.

(c) *When the Pool Originator is the Seller.* When a Pool Originator proposes to form a Pool involving a Pool Loan it owns, it must execute the First Lien Position 504 Loan Pool Guarantee Agreement as Pool Originator and as Seller and, consequently, will be subject to all applicable Program Rules

and Regulations pertaining to both roles.

(d) *When the Pool Originator does not own the Pool Loan.* When a Pool Originator proposes to form a Pool involving a Pool Loan it does not own, it must purchase the Loan Interest it proposes to pool from a Seller that owns the whole Pool Loan and that has the servicing rights. The Pool Originator must purchase the Loan Interest and take it into inventory or settle the purchase of the Loan Interest through the CSA concurrently with the formation of the Pool. The entity selling the Loan Interest to the Pool Originator must execute the First Lien Position 504 Loan Pool Guarantee Agreement as Seller and, consequently, will be subject to all applicable Program Rules and Regulations pertaining to a Seller. The Pool Originator must also execute the First Lien Position 504 Loan Pool Guaranty Agreement.

(e) *What CSA must receive prior to Pool formation.* Before the CSA may carry out its responsibilities relating to the formation of a Pool, it must receive:

(1) From the Pool Originator: A properly completed First Lien Position 504 Loan Pool application form, First Lien Position 504 Loan Guarantee Agreement, and any other documentation which SBA may require, if applicable; and

(2) All cost reimbursement due and payable to the CSA prior to Pool formation owed by the Participants participating in the formation of the Pool.

§ 120.1706 Pool Originator's retained interest in Pool.

The Pool Originator must retain an ownership interest in any Pool it has formed that is equal to at least 5% of the aggregate of the total outstanding principal balance of each Pool Loan with a Loan Interest in the Pool as calculated at the time of Pool formation. Such interest will decline with Loan Interest payments, prepayments, defaults and any other early termination. At Pool formation, the CSA will issue the Pool Originator a Pool Originator Receipt evidencing the Pool Originator's retained interest in the Pool. The Pool Originator may not sell, pledge, participate, or otherwise transfer its Pool Originator Receipt or any interest therein for the life of the Pool.

§ 120.1707 Seller's retained Loan Interest.

The Seller must retain a 15% or greater Loan Interest in each of its loans included in a Pool. At Pool formation, the CSA will issue the Seller a Seller Receipt evidencing the Seller's retained ownership in the Pool Loan. With SBA's written permission, the Seller may sell the Seller Receipt and Servicing Retention Amount in whole, but not in part, to a single entity at one time. The Seller may not sell less than 100% of the Seller Receipt and Servicing Retention Amount, and may not sell a participation interest in any portion of any of its Pooled loans. In addition, in order to complete such sale, Seller must have the purchaser of its rights to the Pool Loan execute an allonge to the Seller's First Lien Position 504 Loan Pool Guarantee Agreement in a form acceptable to SBA, acknowledging and accepting all terms of the Seller's First Lien Position 504 Loan Pool Guarantee Agreement, and deliver the executed original allonge and a copy of the corresponding First Lien Position 504 Loan Pool Guarantee Agreement to the CSA. All Pool Loan payments related to a Seller Receipt and Servicing Retention Amount proposed for sale will be withheld by the CSA pending SBA acknowledgement of receipt of all executed documents required to complete the transfer.

[74 FR 56093, Oct. 30, 2009, as amended at 82 FR 39506, Aug. 21, 2017]

§ 120.1708 Pool Certificates.

(a) *SBA Guarantee of Pool Certificates.* SBA guarantees to a Pool Investor the timely payment of principal and interest installments and any prepayment or other recovery of principal to which the Pool Investor is entitled. If an Obligor misses a scheduled payment pursuant to the terms of the Pool Note underlying a Loan Interest backing a Pool Certificate, SBA, through the CSA, will make advances to maintain the schedule of interest and principal payments to the Pool Investor. If SBA makes such payments, it is subrogated fully to the rights satisfied by such payment.

(b) *SBA guarantee backed by full faith and credit.* SBA's guarantee of the Pool Certificate is backed by the full faith and credit of the United States.

(c) *SBA purchase of a Loan Interest.* SBA will determine whether to purchase a Loan Interest backing a Pool Certificate with an underlying Pool Note that is 60 days or more in arrears. SBA reserves the right to purchase a Loan Interest from a Pool at any time.

(d) *Self-liquidating.* A Pool Certificate represents a fractional beneficial interest in a Pool that is self-liquidating by Pool Loan Receivables and/or SBA Loan Interest payment or redemption.

(e) *Pool Certificate form.* The CSA prepares the Pool Certificate. SBA must approve the form and terms of the Pool Certificate.

(f) *Pool Certificate registration.* A Pool Certificate must be registered with the CSA.

(g) *Face amount of Pool Certificate.* The face amount of a Pool Certificate cannot be less than a minimum amount as specified in the Guide, and the dollar amount of Pool Certificates must be in increments which SBA will specify in the Guide (except for one Pool Certificate for each Pool). SBA may change these requirements based upon an analysis of market conditions and program experience, and will publish any such change in the FEDERAL REGISTER.

(h) *Basis of payment for Pool Certificates.* All payments on a Pool Certificate are due pursuant to terms, conditions, and percentages set forth or referenced therein and are based on the unpaid principal balance of the Pool represented by the Pool Certificate. Any Pool Loan Receivables applicable to a Loan Interest in the SBA-guaranteed portion of a Pool will be passed through to the appropriate Pool Investors with the regularly scheduled payments to such Pool Investors.

(i) *Pool Certificate interest rate.* A Pool Certificate must have a Weighted Average Interest Rate.

(j) *Pool Certificate maturity.* A Pool Certificate must have a Maturity and a Weighted Average Maturity.

(k) *Early Pool Certificate redemption.* SBA, or the CSA on behalf of SBA, may redeem a Pool Certificate prior to its Maturity because of Obligor prepayment and/or SBA purchase of all Loan Interests in the Pool backing the Pool Certificate.

§ 120.1709 Transfers of Pool Certificates.

(a) *Transfer of Pool Certificates.* A Pool Certificate is transferable. A transfer of a Pool Certificate must comply with Article 8 of the Uniform Commercial Code of the State of New York. The seller may use any form of assignment acceptable to SBA and the CSA. The CSA may refuse to issue a Pool Certificate until it is satisfied that the documents of transfer are complete.

(b) *Transfer on CSA records.* In order for the transfer of a Pool Certificate to be effective, the CSA must reflect the transfer on its records.

(c) *Contents of letter of transmittal for Pool Certificate.* A letter of transmittal must accompany each Pool Certificate which a Pool Investor submits to the CSA for transfer. The Pool Investor must supply the following information in the letter:

(1) Pool number;

(2) Pool Certificate number;

(3) Name of purchaser of Pool Certificate;

(4) Address and tax identification number of the purchaser;

(5) Name, e-mail address and telephone number of the person handling or facilitating the transfer; and

(6) Instructions for the delivery of the new Pool Certificate.

(d) *CSA transfer cost recovery.* At the same time a Pool Investor submits a letter of transmittal for a Pool Certificate pursuant to this section, it must send to the CSA sufficient funds to cover its cost for this service. The CSA will supply the transfer information to the Pool Investor.

§ 120.1710 Central servicing of the Program.

(a) *Pool Certificates and Receipts issued at Pool formation.* As part of its role as Central Servicing Agent for the Pool, at Pool formation, CSA issues a Seller Receipt to the Seller, a Pool Originator Receipt to the Pool Originator, and a Pool Certificate to each Pool Investor.

(b) *CSA fiscal transfer responsibilities.* All Pool Loan Receivables on a Pool

Loan received by the CSA must be forwarded by it to pay the Servicing Retention Amount, Ongoing Guarantee Fee, Seller Receipt, Pool Originator Receipt, Pool Certificates, any SBA-purchased Loan Interest, and any other payment applicable to the Pooling of such Pooled Loan, in accordance with Program Rules and Regulations.

(c) *Administration of the Pool Certificates.* CSA must administer each Pool Certificate. It shall maintain a registry of Pool Investors and other information as SBA requires. CSA registers all Pool Certificates. This means it issues, transfers title to, and redeems them. It shall maintain a registry of Pool Investors and other information as SBA requires. In fulfilling its obligation to keep the central registry current, the CSA may, with SBA's approval, obtain any necessary information from the parties involved in the Program.

(d) *CSA Monthly Report.* CSA must provide SBA with a list, by Pool, of each Loan Interest with an underlying Pool Note that is 60 days or more in arrears on a monthly basis.

§ 120.1711 Suspension or termination of Program participation privileges.

(a) *Participant suspension or termination.* The SBA may suspend or terminate the privilege of a Participant, and/or any Associate or Affiliate of the Participant, to sell, purchase, broker, or deal in Pool Loans, Loan Interests, or Pool Certificates under the Program if any such Participant or its Associate or Affiliate has:

(1) Failed to comply materially with any requirement imposed by the Program Rules and Regulations or other SBA rules and regulations; or

(2) Made a material false statement or failed to disclose a material fact to SBA.

(b) *Additional rules for suspension or termination of Pool Originator.* In addition to the conditions set forth in paragraph (a) above, SBA may also suspend or terminate the Program participation privileges of a Pool Originator if the Pool Originator (and/or its Associates):

(1) Does not comply with any of the requirements in 120.1703(a) or (c);

(2) Has been revoked or suspended it from engaging in the securities business by its supervisory agency, or is under investigation for a practice which SBA considers, in its sole discretion, to be relevant to its fitness to participate in the Program;

(3) Has been indicted or otherwise formally charged with, or convicted of, a felony, or a misdemeanor which, in SBA's sole discretion, bears on its fitness to participate in the Program;

(4) Has received an adverse civil judgment that it has committed a breach of trust or a violation of a law or regulation protecting the integrity of business transactions or relationships; or

(5) Has been suspended or terminated as a Pool Assembler under 120.631.

(c) *Suspension procedures.* SBA may undertake suspension or enforcement actions under this section using the procedures set forth in § 120.1600(a).

§ 120.1712 Seller responsibilities with respect to Seller's Pool Loan.

Seller shall remain obligated for servicing and liquidating Seller's Pool Loan until the Pool Loan is repaid in full unless SBA provides written approval or notice to the contrary.

§ 120.1713 Seller's Pool Loan origination.

SBA is entitled to recover from the Seller losses incurred by SBA on its guarantee of a Pool if such losses resulted because Seller's Pool Loan was not made and closed in a commercially reasonable manner, consistent with prudent lending standards, and in accordance with any applicable Program Rules and Regulations.

§ 120.1714 Seller's Pool Loan servicing.

Subject to § 120.1718 of this subpart J, the Seller must service Seller's Pool Loan in a commercially reasonable manner, consistent with prudent lending standards, and in accordance with applicable Program Rules and Regulations. The Seller receives the Servicing Retention Amount for servicing the Seller's Pool Loan.

§ 120.1715 Seller's Pool Loan liquidation.

Subject to § 120.1718 of this subpart J, the Seller must liquidate and conduct debt collection litigation for Seller's Pool Loan in a prompt, cost-effective

and commercially reasonable manner, consistent with prudent lending standards, in accordance with applicable Program Rules and Regulations, and with SBA approval of a liquidation plan and any litigation plan, and any amendment of either such a plan, if applicable.

§ 120.1716 Required SBA approval of servicing actions.

Seller shall not, without prior written consent of SBA, take the following actions with respect to Seller's Pool Loan:

(a) Make or consent to any substantial alteration in the terms (''substantial'' includes, but is not limited to, any changes to the principal amount or interest rate);

(b) Accelerate the maturity;

(c) Sue; or

(d) Waive or release any claim. Guidance on other servicing actions, some of which may need prior SBA approval, is provided in the Guide.

§ 120.1717 Seller's Pool Loan deferments.

Without the prior written consent of SBA, Seller, at the request of Obligor, may grant one deferment of Obligor's scheduled payments for a continuous period not to exceed three months of past or future installments. Seller shall immediately notify CSA of any payment deferment and that notification shall include:

(a) The SBA Pool Loan number;

(b) The Obligor's name;

(c) The terms of such deferment;

(d) The date Obligor is to resume payment; and

(e) Reconfirmation of the basis of interest calculation (e.g. 30/360 or Actual Days/365).

§ 120.1718 SBA's right to assume Seller's responsibilities.

SBA may, in its sole discretion, undertake the servicing, liquidation and/or litigation of Seller's Pool Loan at any time and, in such event, Seller must take any steps necessary to facilitate the assumption by SBA of such responsibilities, which can be transferred by SBA at its discretion to a contractor, agent or other entity, and such steps shall include, among other things, providing or assigning to SBA any documents requested by SBA within 15 calendar days of Seller's receipt of such request. SBA will notify the Obligor of the change in servicing.

§ 120.1719 SBA's right to recover from Seller.

SBA is entitled to recover from Seller any monies paid on SBA's guarantee of a Pool Certificate backed in part by Seller's Pool Loan, plus interest, if SBA in its sole discretion determines that any of the following events has occurred:

(a) Seller's improper action or inaction has put SBA at risk;

(b) Seller has failed to disclose a material fact to SBA regarding a Seller's Pool Loan in a timely manner;

(c) Seller has misrepresented a material fact to SBA regarding Seller's Pool Loan;

(d) Seller has failed to comply materially with § 120.1720 of this subpart;

(e) SBA has received a written request from Seller to terminate the SBA's guarantee on the Loan Interest in Seller's Pool Loan;

(f) Seller has failed to comply materially with Program Rules and Regulations; or

(g) Seller has failed to make, close, service or liquidate Seller's Pool Loan in a prudent manner.

§ 120.1720 SBA's right to review Pool Loan documents.

In the event that SBA purchases a Loan Interest in Seller's Pool Loan, Seller must provide to SBA copies of the Pool Loan collateral documents, Pool Loan underwriting documents, and any other documents SBA may require in writing within 15 calendar days of a written request from SBA (which SBA will review in connection with its efforts to determine if Seller is obligated to reimburse SBA pursuant to this subpart). A Seller's failure to provide the requested documentation may constitute a material failure to comply with the Program Rules and Regulations and may lead to an action for recovery under § 120.1719. SBA will also evaluate a Seller's continued participation in the Program and may restrict further sales under the Program

until SBA determines that the Seller has provided sufficient documentation.

§ 120.1721 SBA's right to investigate.

SBA may undertake such investigation as it deems necessary to determine whether it is entitled to seek recovery from the Seller and Seller agrees to take whatever actions are necessary to facilitate such investigation.

§ 120.1722 SBA's offset rights.

SBA shall have the right to offset any amount owed by Lender to SBA, including, without limitation, an offset against CSA's obligation to pay Lender pursuant to any Section 504 First Mortgage Loan Pool Guarantee Agreement.

§ 120.1723 Pool Loan receivables received by Seller.

Any Pool Loan Receivables received by Seller in connection with obligations under Seller's Pool Loan must be forwarded by Seller to CSA within two business days of receipt of collected funds.

§ 120.1724 Servicing and liquidation expenses.

All ordinary and reasonable expenses of servicing and liquidating Seller's Pool Loan shall be paid by, or be recoverable from, Obligor, and all such ordinary and reasonable expenses incurred by Seller or SBA which are not recoverable from Obligor shall be shared ratably by Seller, SBA, and the Pool Originator pursuant to the applicable percentages set forth in the First Lien Position 504 Loan Pool Guarantee Agreement.

§ 120.1725 No Program Preference by Seller or Pool Originator.

The Seller and the Pool Originator must not establish a Program Preference, which is defined in 13 CFR 120.10.

§ 120.1726 Pool Certificates a Seller cannot purchase.

Neither a Seller, nor any of its Program Associates or Affiliates, may purchase a Pool Certificate that is backed by a Loan Interest in a Pool Loan that the Seller, or any of its Program Associates or Affiliates, originated or owned, and, in the event such purchase occurs, SBA's guarantee shall not be in effect with respect to any such Pool Certificate.

PART 121—SMALL BUSINESS SIZE REGULATIONS

Subpart A—Size Eligibility Provisions and Standards

PROVISIONS OF GENERAL APPLICABILITY

SIZE STANDARDS USED TO DEFINE SMALL BUSINESS CONCERNS

SIZE ELIGIBILITY REQUIREMENTS FOR SBA FINANCIAL ASSISTANCE

SIZE ELIGIBILITY REQUIREMENTS FOR GOVERNMENT PROCUREMENT