

**12 CFR Part 11**

Confidential business information, National banks, Reporting and recordkeeping requirements, Securities.

**12 CFR Part 16**

National banks, Reporting and recordkeeping requirements, Securities.

**12 CFR Part 19**

Administrative practice and procedure, Crime, Equal access to justice, Investigations, National banks, Penalties, Securities.

**12 CFR Part 24**

Community development, Credit, Investments, Low and moderate income housing, National banks, Reporting and recordkeeping requirements, Rural areas, Small businesses.

**12 CFR Part 34**

Mortgages, National banks, Reporting and recordkeeping requirements.

**12 CFR Part 40**

Banks, Banking, Consumer protection, National banks, Privacy, Reporting and recordkeeping requirements.

For the reasons set forth in the preamble, and under the authority of 12 U.S.C. 93a, chapter I of title 12 of the Code of Federal Regulations is amended as follows:

**PART 4 [AMENDED]**

- 1. Part 4 is amended as follows:
- a. Remove the phrase “250 E Street, SW.” wherever it appears and add “400 7th Street SW.” in its place in §§ 4.4, 4.14(c), and 4.17(c);
- b. Remove the phrase “250 E Street, SW.” and add “400 7th Street, SW.” in its place in §§ 4.15(b)(1), 4.15(e)(2), and 4.34(a);
- c. Remove the web address “<https://appsec.occ.gov/publicaccesslink/palMain.aspx>” and add the web address “<https://foia-pal.occ.gov/palMain.aspx>” in its place in §§ 4.15(b)(1), 4.18(a)(1), and 4.18(b); and
- d. Remove the phrase “OCC Communications Division” and add in its place “Disclosure Services, Communications Division” in § 4.15(g).

**PART 5 [AMENDED]**

- 2. Part 5 is amended as follows:
- a. Remove the phrase “250 E Street SW., Washington, DC 20219–0001” and add “400 7th Street SW., Washington, DC 20219” in its place in § 5.2(c);
- b. Remove the web address “<http://www.occ.treas.gov>” and add “[www.occ.gov](http://www.occ.gov)” in its place in § 5.2(c); and

- c. Remove the web address “[www.occ.treas.gov](http://www.occ.treas.gov)” and add “[www.occ.gov](http://www.occ.gov)” in its place in footnote 1 in § 5.34(e)(5)(v)(R).

**PART 7 [AMENDED]**

- 3. Part 7 is amended by removing the phrase “250 E Street SW.” and adding “400 7th Street SW.” in its place in footnote 2 in § 7.2000(c).

**PART 10 [AMENDED]**

- 4. Part 10 is amended by removing the phrase “250 E Street SW.” and adding “400 7th Street SW.” in its place in § 10.2(c).

**PART 11 [AMENDED]**

- 5. Part 11 is amended by removing the phrase “250 E Street SW.” and adding “400 7th Street SW.” in its place in § 11.3(a)(1).

**PART 16 [AMENDED]**

- 6. Part 16 is amended by removing the phrase “250 E Street SW.” and adding “400 7th Street SW.” in its place in § 16.17(a).

**PART 19 [AMENDED]**

- 7. Part 19 is amended by removing the phrase “250 E Street SW.” and adding “400 7th Street SW.” in its place in § 19.100.

**PART 24 [AMENDED]**

- 8. Part 24 is amended by removing the web address “<http://www.occ.treas.gov>” and adding “[www.occ.gov](http://www.occ.gov)” in its place in § 24.5(a)(2) and (b)(1).

**PART 34—REAL ESTATE LENDING AND APPRAISALS**

- 9. Revise the authority citation for part 34 to read as follows:

**Authority:** 12 U.S.C. 1 *et seq.*, 25b, 29, 93a, 371, 1465, 1701j–3, 1828(o), and 5412(b)(2)(B).

**Subpart F [Removed]**

- 10. Remove subpart F, consisting of §§ 34.101 through Appendix A to Subpart F of Part 34.

**PART 40 [REMOVED]**

- 11. Remove part 40.

Dated: March 10, 2014.

**Thomas J. Curry,**  
*Comptroller of the Currency.*

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**SMALL BUSINESS ADMINISTRATION****13 CFR Part 120**

**RIN 3245–AG04**

**504 and 7(a) Loan Programs Updates**

**AGENCY:** U.S. Small Business Administration.

**ACTION:** Final rule.

**SUMMARY:** This rule finalizes the proposed rule that the U.S. Small Business Administration (“SBA”) issued to improve access to its two flagship business lending programs: the 504 Loan Program and the 7(a) Loan Program. This rule will enhance job creation through increasing eligibility for loans under SBA’s business loan programs and by modifying certain program participant requirements applicable to the 504 Loan Program. In addition, SBA is revising Certified Development Company (CDC) operations requirements to clarify certain existing regulations. SBA has decided to further study the issue of how to redefine affiliation for the business loan programs and is not including any changes to the affiliation standards in this final rule.

**DATES:** This rule is effective April 21, 2014, except for the amendment to 13 CFR 120.823, which is effective April 21, 2015.

**FOR FURTHER INFORMATION CONTACT:** Linda Rusche, Director, of Financial Assistance; ATTN: Linda Reilly, Chief, 504 Program Branch, Office of Financial Assistance, Small Business Administration, 409 3rd Street SW., Washington, DC 20416; telephone 202–205–9949.

**SUPPLEMENTARY INFORMATION:****I. Background**

The 504 Loan Program and 7(a) Loan Program are SBA’s two primary business loan programs authorized under the Small Business Investment Act of 1958 and the Small Business Act, respectively. On February 25, 2013, SBA published a proposed rule with request for comments in the **Federal Register** to implement several changes intended to reinvigorate the business loan programs by eliminating unnecessary compliance burdens and loan eligibility restrictions. 78 FR 12633. The major changes proposed by SBA related to affiliation principles, the personal resources test, the 9-month rule for the 504 Loan Program, and operational and organizational requirements for Certified Development Companies (“CDCs”). The comment period was open until April 26, 2013. SBA received

99 written comments during the comment period. These comments were received from 62 separate entities or individuals, including 32 CDCs, 16 financial institutions, 11 trade associations, one business, one United States Senator, and one individual. (The number of separate commenters does not total 99 because, in many cases, SBA received more than one submission from representatives of the same entity). The comments are summarized and addressed below.

## II. Summary of Comments Received

### A. Affiliation as Applied to the Business Loan Programs—Section 121.302

SBA received 56 comments related to the proposed affiliation standards for small businesses. SBA received many comments that were generally supportive of the proposed standards and also received several comments that opposed or suggested modifications to certain provisions. Several commenters opposed the “totality of the circumstances” standard set forth in proposed section 121.302(a). Among the comments were that this standard would leave too much gray area and might not be consistently applied, and that it would be preferable to have a black and white test; that this standard is vague and open-ended; and that it would subject lender decisions to more scrutiny and second-guessing than currently occurs. In addition, many commenters expressed concern that the proposed six-page Applicant Affidavit on Affiliation was far too complicated for the typical applicant to complete without the extensive assistance of an attorney, a certified public accountant, and/or the CDC. Some expressed concern that the proposed Affidavit would likely add to the applicant’s cost and would increase the time needed to prepare applications, and would not, contrary to SBA’s intention, result in streamlining the process and reducing costs. Another commenter stated that the CDC would not be able to rely exclusively on the Affidavit, and would still be required by prudent lending to evaluate the validity of the Affidavit by comparing it to the applicant’s financial and organizational documents. In light of the comments, and upon further consideration, SBA has decided to further study the issue of redefining affiliation for the business loan programs and is not finalizing any changes to the affiliation standards at this time.

### B. Elimination of Personal Resources Test in Business Loan Programs—Section 120.102

SBA proposed to eliminate section 120.102, commonly known as “the personal resources test.” Commenters expressed overwhelming support for the elimination of this regulation, which requires certain owners of a Borrower to inject personal liquid assets into the business to reduce the amount of SBA guaranteed funds that would otherwise be needed. Those opposed to eliminating the regulation were concerned that it would lead to increased scrutiny by SBA of lenders’ determinations that credit was “not available elsewhere”, which is a requirement of Section 120.101. While there may be some connection between Section 120.101 and 120.102, the findings for each are distinct. The present regulation at Section 120.102 concerns the effect of personal resources available to the applicant, while the regulation at Section 120.101 addresses the availability of financing from non-federal sources. Others opposed felt that more Borrowers with significant assets would receive loans and that personal liquid assets would not be required to be converted to collateral for the loan, and that this practice would not be consistent with prudent lending. Although SBA will no longer require that the personal resources of owners be used to reduce the SBA funded portion of the total financing package, a lender that believes that prudent lending requires that assets either be injected or pledged as collateral for a particular loan would not be prohibited from so requiring. See, e.g., 13 CFR 120.150.

One commenter suggested that SBA raise the level of exempted personal resources rather than eliminate the rule entirely. SBA considered that option but determined that elimination of the personal resources test would enable more robust Borrowers to participate in SBA’s loan programs, thus mitigating risk to SBA’s loan portfolio while facilitating job growth. SBA is adopting this regulation as proposed by removing this provision from the regulations.

### C. CDC Operational and Organizational Requirements

#### 1. Section 120.816 CDC Non-Profit Status and Good Standing

SBA proposed to redesignate section 120.820 as section 120.816. There were no comments regarding this change, and SBA is redesignating this section as proposed.

#### 2. Section 120.818 Applicability to Existing for-Profit CDCs

SBA proposed to add this section to clarify that, unless expressly provided otherwise in the regulations, any Loan Program Requirement (as defined in section 120.10) that applies to non-profit CDCs also applies to for-profit CDCs. This regulation reflects current practice. All commenters supported this regulation, but one commenter suggested that the rule be modified to permit for-profit CDCs to pay dividends. However, under current section 120.825, CDCs are prohibited from paying dividends out of funds generated from loan activity in the 504 Loan Program. This regulation requires that any funds generated from 504 loan activity by a CDC that remain after payment of staff and overhead expenses 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. This requirement serves the interests of the 504 Loan Program, and SBA will not modify the rule to permit dividends.

The commenter also suggested that the rule be modified to allow shareholders to serve as officers, directors and employees. However, under current section 120.823, a shareholder may be an employee or staff of a CDC, but may not at the same time serve as a voting member of the Board. SBA is continuing this prohibition in the final rule.

SBA has required that CDCs be non-profit corporations since 1987 (see current 13 CFR 120.820). There are five for-profit CDCs that were established and certified by SBA prior to that date, and these CDCs have been allowed to continue to operate in the 504 Loan Program. As noted above, this section is expressly stating the existing practice, which SBA believes is appropriate, and SBA is adopting this regulation as proposed.

#### 3. Section 120.820 CDC Affiliation

In section 120.820(a), SBA proposed to require that a CDC be independent and not affiliated with any Person (the definition of which under § 120.10 includes a 7(a) Lender), except as permitted under this section. No comments were received with respect to paragraph (a), and SBA is adopting this provision as proposed.

In section 120.820(b), SBA proposed to permit CDCs to be affiliated with an entity 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 political subdivision. SBA

received several comments in support of this provision. However, one commenter expressed concern that the affiliated entity could charge the CDC excessive fees. SBA also received two comments in opposition from CDCs that currently each have a for-profit affiliate. These commenters stated that the for-profit affiliate needed to associate with a community development or economic development partner in order to secure other federal financial assistance, such as through the New Market Tax Credits Program. One of the commenters stated that, through its for-profit affiliate, the CDC derived additional income that it was able to use to invest in economic development activities in its community, including to provide financial and professional technical assistance to disadvantaged small businesses. Both commenters also requested that SBA consider revising the rule to include a “grandfather provision”, arguing that it would be unfair to apply this prohibition to existing for-profit affiliates.

SBA has considered these comments and is revising the final rule to add a new paragraph (e) to allow a CDC to continue to have for-profit affiliates (other than a 7(a) Lender) if such for-profit entities were affiliated with the CDC prior to the date of publication of this final rule in the **Federal Register**. In addition, SBA recognizes that, after the effective date of this final rule, there may be unique circumstances, such as those described by the commenters, where a CDC’s affiliation with a for-profit entity may serve the best interests of the 504 Loan Program. Accordingly, SBA is revising the rule to provide that, with the prior written approval of the D/FA or designee in his or her discretion, a CDC may be affiliated with a for-profit entity (other than a 7(a) Lender) whose function is economic development in the same Area of Operations if such affiliation is in the best interests of the 504 Loan Program.

With respect to section 120.820(c), a few commenters generally supported this provision which, as proposed, would permit a CDC to continue its affiliation with a 7(a) Lender that is either a state or local development company approved by SBA as of November 6, 2003, or a credit union, so long as the affiliation was in effect as of the effective date for this final rule. For the final rule, SBA is simplifying this provision to state that “[a] CDC that was affiliated with a 7(a) Lender as of November 6, 2003, may continue such affiliation.” This change retains the timeframe for grandfathering affiliations with state development companies that is contained in section 120.852(a)—

which allows for such affiliations if they existed as of November 6, 2003—instead of extending the grandfather period for these affiliations to the effective date of this final rule. This change would also allow a CDC to continue to be affiliated with any other 7(a) Lender (including credit unions) if the affiliation was in effect as of November 6, 2003. SBA does not expect that changing the grandfather period for these 7(a) Lenders from the effective date of this final rule to November 6, 2003 will affect any CDCs. The limited grandfathering of pre-existing affiliations between CDCs and 7(a) Lenders set forth in this provision is the only exception to the prohibition on these affiliations that is authorized under SBA’s rules.

In addition, SBA is including in section 120.820(c) the prohibition against a CDC affiliating with or investing, directly or indirectly, in a 7(a) Lender. This prohibition is currently set forth in § 120.852(a) and, to avoid confusion, SBA is consolidating all of the provisions related to CDC affiliation in section 120.820. SBA has long interpreted the prohibition against a CDC investing in a 7(a) Lender to mean investing “directly or indirectly” and is including this phrase in the rule. With this change, and the change discussed below regarding SBICs in section 120.852(b), SBA is removing and reserving § 120.852.

Several commenters were opposed to proposed section 120.820(d), in which SBA proposed to prohibit CDCs from being affiliated with, or directly or indirectly investing in or financing, another CDC. The commenters stated that the program has benefited from more experienced CDCs being able to offer financial or managerial assistance to new CDCs. One commenter expressed concern that this provision would prohibit a CDC from contracting with another CDC for “back-office packaging, processing or liquidation services”. SBA recognizes that the program may benefit from such assistance and, under current section 120.824(b), a CDC may continue to request SBA’s approval of a professional services contract with another CDC. However, SBA does intend for section 120.820(d) to prohibit a CDC from being affiliated with another CDC. To clarify how affiliation would be determined, SBA is adding the phrase “as determined in accordance with 121.103” to this provision. SBA would not expect that contracts between CDCs that are for limited services would give rise to affiliation under section 121.103 and be prohibited by this provision. The question of whether a contract for more extensive services would give rise to affiliation would depend on the specific

facts presented by that contract and would need to be determined by SBA on a case-by-case basis.

With respect to this provision’s prohibition on a CDC directly or indirectly investing in or financing another CDC, some commenters suggested that SBA allow a CDC to so invest in or finance another CDC with SBA’s prior written approval. SBA agrees with this recommendation and is amending this provision to so provide.

As discussed above, to complete the consolidation of the provisions related to CDC affiliation in § 120.820, SBA is moving the provision set forth in § 120.852(b), which prohibits a CDC from investing directly or indirectly in an SBIC, to § 120.820 as paragraph (f). Finally, SBA has made additional edits throughout the section for clarification purposes.

#### 4. Section 120.822 CDC Membership

SBA proposed eliminating the membership requirement for CDCs. Most commenters who submitted comments on this provision expressed support for this change because they believe that maintaining membership is unproductive for the CDC. Several commenters who opposed the change did so on three bases, including that members were a valuable resource to CDCs providing them with insight into local communities, that 501(c)(6) organizations, such as some CDCs, were required by the IRS to be membership based, and that not requiring membership in each state where a CDC is located may encourage the expansion of more CDCs into a state, resulting in a dilution of the pool of small business applicants within the state.

SBA notes that there is nothing in the regulations as proposed that would preclude CDCs from deciding to have a membership. If the organization is required by the IRS to have members, or if for some other reason it chooses to have members, the CDC may do so. SBA is simply removing the requirement that a CDC have a membership. SBA also notes that the same concern about the pool of small business applicants being diluted was raised when SBA allowed CDCs to expand their Area of Operations within an entire State, and this concern has not been realized. In addition, the concern regarding the need for a connection to the local community will continue to be addressed by the requirements that a multi-state CDC create loan committees in each State in which the CDC operates and that loan committee members must 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. The final rule, therefore, removes section 120.822, as proposed.

#### 5. Section 120.823 CDC Board of Directors

SBA received many comments on Section 120.823, in which SBA proposed several changes with respect to the requirements that apply to the CDC Board of Directors.

Section 120.823(a) primarily addresses the size of the Board and areas of expertise for directors. SBA proposed to require that the size of the CDC Board of Directors be no fewer than 11 and no more than 25 members; that the Board have directors with background and expertise in internal controls, risk management, commercial lending, legal issues related to commercial lending and corporate governance; and that the CDC Board have at least one director from the economic, community or workforce development field and two directors that are representatives from the commercial lending field. In addition, the rule proposed to permit the directors to be either active in or retired from their fields.

Many commenters opposed the limitation of the Board size from 11–25 both on the basis that the lower limitation was too high and that the higher limitation was too low. After considering the comments, SBA has determined that it will amend this provision to lower the minimum number from 11 to 9, and will also allow CDCs to request SBA's approval to have fewer than 9 directors. Some commenters expressed a legitimate concern that CDCs in rural or isolated communities may have difficulty in finding people to serve and may have other valid reasons that would justify having fewer directors. SBA will also give CDCs the flexibility to create a Board with more than 25 directors by revising the rule to reflect that the upper number of 25 is not a requirement but a recommendation.

A majority of the commenters who submitted comments on this provision supported the rule's minimum requirements regarding the background and expertise of directors, but some requested clarification as to whether one director could have more than one area of expertise. Certainly, a director may have a background in more than one area and, thus, be qualified as an expert in more than one area. Commenters opposed to the rule argued that CDCs may obtain any expertise needed through professional services contracts. SBA believes, however, that it is important that these areas of expertise

be represented on the Board. All commenters supported allowing retired individuals to represent the fields from which they are retired. SBA is adopting this provision as proposed with the exception of changing the Board size requirements as described above.

With respect to section 120.823(b), many commenters supported the requirement proposed by SBA to increase the number of Board members with commercial lending experience (other than the CDC manager) from one to two. Commenters opposed to this requirement expressed concern that it would be difficult to find more than one commercial lender to sit on the Board. However, SBA believes that Board members with commercial lending experience add the necessary expertise for approving loans.

Other commenters opposed to this requirement stated that two members with such expertise would be insufficient for the Board. However, a CDC is not restricted to having only two members with commercial lending experience. A CDC may have more such members, so long as the number is less than 50% of the representation on the Board. Indeed, in order to comply with the voting requirements, a CDC may need to have more than two such directors if one of the directors must recuse him or herself from the vote. SBA is adopting this provision as proposed.

With respect to section 120.823(c), most commenters supported the proposed requirement that the CDC Board of Directors meet at least quarterly and be responsible for any actions of the CDC and any committees established by the Board. One CDC commenter opposed the language because its Board meets monthly. However, there is nothing in the regulation to prohibit the Boards of Directors from meeting more frequently, and SBA is adopting the introductory clause of section 120.823(c) as proposed.

In section 120.823(c)(1), SBA proposed that no CDC staff member except the CDC manager could be a voting member of the CDC Board. SBA received no comments regarding paragraph (c)(1), and is adopting the paragraph as proposed.

With respect to section 120.823(c)(2), SBA proposed to require that a CDC set a quorum of not less than 50% of the Board of Directors. The majority of the commenters supported the changes to this provision, but there was a single request for modifying the requirement for a quorum to 40%. However, SBA believes that a 50% quorum is standard business practice, and is adopting this paragraph as proposed.

With respect to section 120.823(c)(3), all of the comments supported the proposed change, which would permit the attendance at meetings through any format permitted by state law. This provision recognizes that there are now methods for meeting other than being physically present, and SBA is adopting this paragraph as proposed.

With respect to section 120.823(c)(4), most of the comments received in response to this provision supported SBA's proposal to limit the number of directors in the commercial lending field to less than 50% of the Board of Directors. Some requested that SBA raise the percentage to 60 or 67%. One commenter opposing the change stated that commercial lenders are especially well-qualified to serve on a CDC Board and should comprise a larger percentage of the Board. While SBA understands the commenters' points of view, SBA believes that CDCs will be better served by having a more diverse Board not dominated by commercial lenders and is adopting this paragraph as proposed.

With respect to section 120.823(c)(5), SBA proposed to limit the ability of an outside entity to control a CDC's Board by restricting a single entity's representation on the Board to one member. The majority of the commenters was opposed to or requested modification of this paragraph based primarily upon their mistaken interpretation that this provision would prohibit any member of the CDC's Board of Directors from serving on the Board of any other entity. SBA does not intend for this provision to have that effect, but to only prohibit more than one member of the CDC's Board of Directors to be employed by or serve on the Board of Directors of any other single entity (including the entity's affiliates). SBA is revising this provision to clarify this intent.

In addition, one commenter expressed concern that paragraph (c)(5) would prohibit more than one board member of a CDC from serving on the board of the same civic organization, such as a Rotary Club. However, SBA has no objection to more than one board member serving on the same board of a civic, charitable, or comparable entity, provided the entity is not involved in financial services or economic development activities. SBA is amending the rule to clarify this intention. SBA is also making a technical change to clarify that no CDC Board member may serve on the Board of another CDC, in accordance with current § 120.851(b).

With respect to section 120.823(d), SBA proposed to require that the Board be responsible for ensuring that the

structure and operation of the CDC comply with SBA's Loan Program Requirements. In paragraphs (d)(1) and (2), SBA proposed to require that the Board be responsible for setting the mission and hiring, firing, supervising and evaluating the CDC manager. To emphasize the fiscal responsibility of the Board as it relates to salaries, paragraph (d)(3) explicitly outlines the duties of the Board to set salaries for the CDC manager and to review all other salaries to provide greater transparency and accountability. SBA would require that a Report on Compensation be included in the Annual Report (see proposed § 120.830). SBA also proposed in paragraph (d)(4) to provide the CDC with flexibility in determining whether to have committees, but addressed the requirements for Executive and Loan Committees, if established.

Many commenters expressed overall support for paragraphs (d)(1)–(4). A few commenters requested modification or clarification and expressed concern that these paragraphs, generally, placed too much responsibility on the Board of Directors. For example, section 120.823(d)(3) requires that the Board set the CDC manager's salary and review all other salaries, and one commenter suggested that this regulation would require the Board to set all salaries. However, this provision only requires that the Board set the salary for the CDC manager and review the salaries set by that manager. Moreover, the Board of Directors of an organization is generally responsible for all actions of that organization.

In addition, in response to the comments that expressed concern about the need for CDCs to maintain a connection to the local community, SBA is revising section 120.823(d)(4)(ii) to include a new paragraph (E) that retains the current requirement that the Loan Committee consist of 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.

No specific comments were submitted as to paragraphs 120.823(d)(5)–(9). With respect to section 120.823(d)(5), SBA proposed to require that the Board ensure that the CDC's expenses are reasonable and customary, and in section 120.823(d)(6), SBA proposed to require the Board to hire an independent auditor to provide financial statements in accordance with the Loan Program Requirements.

The proposed provisions in paragraphs (d)(7) and (8) emphasize the requirement that the Board monitor the portfolio and review the semiannual

status report from the CDC to ensure that the Board provides appropriate oversight of the CDC's portfolio. SBA proposed to add requirements in paragraph (d)(9) that the Board ensure that the CDC establish and maintain adequate reserves to enable the CDC to operate.

SBA is adopting paragraphs 120.823(d)(1)–(9) as proposed.

With respect to section 120.823(d)(10), SBA proposed to require the Board to approve all investments over \$2,500. Most commenters opposed or requested modification to this paragraph. The commenters expressed concern that the amount was too low and suggested that when the Board approves the budget, it approves each investment. Other CDCs commented that they have other loan programs where they manage loan funds in which almost every action would involve funds of over \$2,500. After review, SBA agrees with the suggestion and is amending the regulation to provide that the Board must approve each CDC investment; however, 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.

With respect to section 120.823(d)(11), SBA proposed to require that the Board establish a policy in the Bylaws of the CDC prohibiting an actual or apparent conflict of interest, and enforce such policy. Most commenters supported the policy, but one was opposed based upon the fact that the CDC did not want to be mandated to use a federal definition of "conflict of interest." Several other CDCs recommended that SBA not require the policy to be placed in the Bylaws. SBA did not specifically define "conflict of interest" in this section, but at a minimum the CDC's Bylaws must meet the standards of 13 CFR 120.140. The Bylaws of a corporation are drawn to regulate its management and internal affairs, and it is the Agency's belief that a conflict of interest policy is properly included in the Bylaws. SBA is adopting this paragraph as proposed.

With respect to 120.823(d)(12) and (13), SBA proposed to require the Board to retain accountability for the actions of the CDC, and establish internal control policies in accordance with 13 CFR 120.826. A majority of the commenters supported these policies. One commenter expressed concern that the requirement to establish internal controls required the CDC to hire an outside consultant to monitor internal controls of the CDC. It does not. The

regulation requires that the Board establish the policy. This is not a new requirement as the requirement is fully described in the current regulation at 13 CFR 120.826(b), but is added here to consolidate all of the Board requirements in one section. SBA is adopting paragraphs (12) and (13) as proposed.

With respect to section 120.823(d)(14), SBA proposed to require that the Board establish commercially reasonable loan approval policies, procedures and standards, and include in its Bylaws a credit approval process and any delegations to an Executive Committee or Loan Committee. The majority of commenters opposed the requirement that the credit approval process be set forth in the CDC's Bylaws. SBA has considered these comments and agrees that it would be sufficient to allow the CDC to set forth the credit approval process in a loan policy manual. SBA is amending the proposed rule to reflect these changes.

Two of those opposed also objected to the requirement contained in (d)(14) that the Board ratify or approve loans over a certain dollar amount. SBA believes that it is the Board's responsibility to do so and that the requirement is reasonable and appropriate; therefore, SBA is not changing the approval requirement.

With respect to section 120.823(d)(15), SBA proposed to require that Board members certify annually that they have read and understand Section 120.823 of this regulation. Many commenters supported the paragraph, and some requested modification to either permit a separate governance committee to make the certification or to permit Board members to take training instead. Several commenters opposed the requirement as being too onerous. SBA does not agree with the commenters. Training would be more expensive and time-consuming for the Board members than reading this section of the regulation and signing a certification that they have done so. SBA believes that the annual certification by all Board members that they have read and understand section 120.823 is important and is adopting paragraph (d)(15) as proposed.

With respect to section 120.823(e), SBA proposed to require that CDCs maintain Directors' and Officers' Liability and Errors and Omission insurance in the amount of at least \$5,500,000 (in the aggregate and for each occurrence) with a deductible of not more than \$50,000. SBA invited comments on the amounts of both the insurance and the deductible. No commenters fully supported the

requirement. Twenty-eight CDCs (or 11% of all CDCs), submitted comments on this issue and expressed a concern that this proposed provision would increase the cost of insurance. Some commenters felt that the financial burden on the CDCs was too great because increasing the insurance coverage as required would triple their premiums. One commenter indicated that, while he supported the requirement for insurance, he would recommend that a fee be added to the debenture to cover the cost. Others suggested that there be flexibility as to the deductible, that the amount be left to the Board, or that the amount be based upon portfolio size.

In proposing this insurance requirement that would apply to all CDCs, SBA's intent is to address the higher risks associated with the statutory increases in the 504 loan amounts of up to \$5 million for each small business concern and \$5.5 million for certain projects. As a result of these higher amounts, a CDC's loan volume may increase, which is expected to result in an increase in the processing and servicing fees collected by CDCs that will offset any new costs associated with this new insurance requirement. However, after considering all of the comments, SBA has determined that not all CDCs may need to have insurance coverage of \$5.5 million per occurrence and in the aggregate per year SBA agrees that the amount of insurance should generally correspond to the size of a CDC's portfolio. SBA intends to consult with CDCs and their representatives, as well as insurance underwriters, in developing the appropriate amounts of insurance required. These amounts will not exceed the amount of insurance proposed by SBA in the proposed rule and will not be less than \$1 million. Further guidance on CDC insurance requirements will be in the next update to SOP 50 10 after the final rule is effective.

Finally, several commenters expressed concern regarding the effective date of the changes in section 120.823 and that CDCs would need time to implement the changes. SBA agrees and is delaying the effective date of the changes made to section 120.823 until 12 months after the date of publication in the **Federal Register**, at which time CDCs must be in compliance with this section. In the interim, CDCs must continue to comply with the requirements set forth in current section 120.823.

#### 6. Section 120.830 Reports a CDC Must Submit

SBA proposed to revise the requirements with respect to the reports that a CDC must submit to SBA. In section 120.830(a), SBA proposed to require that a CDC submit with its Annual Report its most recent Federal tax return; audited or reviewed financial statements, as appropriate; a report on compensation of any current or former officer, director, employee or independent contractor who received compensation during the covered period of more than \$100,000; written certification from each of its Directors that each has read and understands the requirements of 13 CFR Section 120.823; and a report on investments in economic development activities in each state in which it has a loan.

Commenters generally supported the requirements. One commenter noted that the IRS Form 990 includes information on compensation for employees earning more than \$100,000 year. SBA agrees that the submission of the IRS Form 990 would satisfy this reporting requirement. Non-profit CDCs that have not yet completed the IRS Form 990 for their last tax year, or for-profit CDCs that are not required by the IRS to file the IRS Form 990, may submit the information in any format as long as it includes all of the information with respect to employee compensation that would be found on the IRS Form 990. One commenter indicated SBA could obtain the requested information by searching for the IRS Form 990 on-line, but the on-line version is often one to two years old and is not acceptable. Another recommended that SBA modify the report on compensation to require the CDC to report any compensation that CDC employees earning more than \$100,000 per year receive not only from the CDC, but also from any outside source. However, even if a CDC had sufficient information to report on the outside compensation received by its employees, SBA is primarily interested in the compensation that CDC employees receive from the CDC, not outside sources. SBA would expect, however, the CDC to provide information on the compensation that CDC directors, officers or employees receive from "related organizations" to the CDC, as required to be reported on the IRS Form 990.

In addition, one commenter suggested that any reimbursement for expenses that the employee receives that the IRS does not include as compensation ("accountable expenses") should not be reported as income for SBA purposes. The commenter observed that the IRS

Form 990 would not include any accountable expenses. SBA agrees that expenses not reportable as compensation to the IRS may be excluded from the CDC's report on compensation.

Finally, with respect to section 120.830(a)(4), several commenters supported the proposed requirement that the report include the economic development investments made in each state in which the CDC has an outstanding loan, but requested clarification with respect to what would constitute economic development. SBA notes that economic development investment in the community could take many forms including, but not limited to, investment in a foundation established for economic development, direct investment through other loan programs in the community, or investment in other economic development entities. SBA would expect the investment report to include each investment by type and amount. SBA is adopting section 120.830 as proposed.

#### 7. Section 120.835 Application To Expand an Area of Operation

SBA proposed eliminating the requirement that a CDC have membership in each state in a Multi-State expansion since the proposed revisions to Section 120.822 make membership optional. A majority of the commenters supported this change. Those opposed expressed the opinion that membership in an area the CDC serves gives it a stronger relationship with each state in a CDC's Area of Operations. In addition, some of the commenters opposed felt that eliminating the requirement for membership in each state would make it easier for a CDC to move into a contiguous state which would dilute the pool of potential projects within each state. As discussed above under section 120.822, similar arguments were made when CDCs were allowed to operate statewide for projects, and that has not proven to be the case. Further, SBA is retaining the requirements in current sections 120.835(c)(3) and 120.823(a) and (b), which together require a multi-state CDC to have a loan committee in each State into which it expands that meets local membership requirements. SBA is adopting this section as proposed.

8. Section 120.852 Restrictions Regarding CDC Participation in the Small Business Investment Company (SBIC) Program and the 7(a) Loan Program

As discussed above, SBA is removing and reserving section 120.852, and moving its content to section 120.820.

9. Section 120.920 Required Participation by the Third Party Lender, and Section 120.925 Preferences

SBA proposed to revise section 120.920 to provide that if a Third Party Lender requires a lien on collateral in addition to the Project Property, the Third Party Lender, in the event of liquidation, must first apply the proceeds from the sale of such additional collateral to the balance on the Third Party Lender's loan. SBA believes that this change could increase recoveries on the 504 loan. Commenters were generally supportive of this change. Some commenters requested that SBA clarify that the Third Party Lender does not have to liquidate collateral that either no longer exists or has no recoverable value. However, this language is in the Third Party Lender Agreement signed by the Third Party Lender, and so there is no need to amend the regulation.

Commenters were also generally supportive of SBA's proposal to eliminate section 120.925 regarding Preferences. However, one commenter was opposed to the elimination of this provision, arguing that the Lender should not be permitted to have any type of Preference. A Preference is defined as "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." See § 120.10 (Definition of "Preference"). SBA recognizes that there are other types of security that the Third Party Lender could obtain for its loan in addition to a lien on additional collateral, such as a guaranty or other arrangements for repayment, and that the Third Party Lender should be required to comply with proposed section 120.920 for this collateral or security as well. Accordingly, SBA is revising section 120.920 to apply the requirements of section 120.920 to any type of collateral or security that the Third Party Lender obtains.

In addition, one commenter requested clarification as to the timing of the sale

of the collateral by the Third Party Lender. Under the proposed regulation, the proceeds of any collateral held in addition to the Project Property must be applied to the Third Party Lender's debt prior to the proceeds of the Project Property. SBA agrees that clarification would be helpful and is amending the final rule to require that, unless otherwise approved in writing by SBA, the Third Party Lender liquidate, or otherwise exhaust all reasonable avenues of collection with respect to, the additional collateral or other security no later than the disposition of the Project Property, and to apply any proceeds received as a result of such 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.

*D. Section 120.882(a)—The "9-Month Rule" (Applies to 504 Loan Program Only)*

With respect to section 120.882(a), SBA proposed to eliminate paragraph (a)(2) of this section which limits Project expenses eligible for 504 Loan Program financing to those incurred within 9 months prior to receipt by SBA of a complete loan application. As explained in the proposed rule, SBA intends for this change to permit financings of expenses toward a Project regardless of when they were incurred, so long as they are directly attributable to the Project. SBA also observed that there may be circumstances when an applicant might incur short term debt to cover expenses directly attributable to a Project that is eligible for financing under the 504 Loan Program. As stated in the proposed rule, SBA believes that determining whether an expense has been incurred by an applicant for a 504 project requires a fact specific analysis which appropriate agency personnel need to make regardless of when the expense was incurred.

All commenters expressed support for this change with one comment seeking clarification as to whether long-term debt could be included in a 504 project. Historically, the 504 Loan Program did not include debt refinancing except in the limited circumstance where the debt was "directly attributable" to the Project and incurred within certain time limitations. For example, under current SBA policy, the 504 loan may refinance short term debt (known as "bridge financing") on the Project land as long as the financing is for a term of 3 years or less. See SOP 50 10 5(F), Subpart C, Chapter 2, Paragraph III.H.4.(a)(2)(b). More recently, the 504 Loan Program was authorized to also permit

refinancing of debt unrelated to the Project so long as the Project involved expansion of a small business concern (120.882(e)) and, on a temporary basis, the refinancing of certain debt with no business expansion required (120.882(g), the authority for which has expired). Accordingly, the only type of debt that SBA permits to be financed other than under § 120.882(e) is "bridge financing" that is directly attributable to the Project, and the elimination of the 9-month rule is not intended to change this policy. SBA will continue to determine whether expenses incurred prior to application were in fact incurred for a 504 Project. SBA is adopting this provision as proposed.

**Compliance With Executive Orders 13563, 12866, 12988, and 13132, the Paperwork Reduction Act (44 U.S.C. Ch. 35), and the Regulatory Flexibility Act (5 U.S.C. 601–612)**

*Executive Order 13563 and Executive Order 12866*

The Office of Management and Budget (OMB) has determined that this final rule is a "significant" regulatory action for the purposes of Executive Order 12866. Accordingly, the next section contains SBA's Regulatory Impact Analysis. However, this is not a major rule under the Congressional Review Act, 5 U.S.C. 800.

*Regulatory Impact Analysis*

SBA provided a detailed Regulatory Impact Analysis in the Proposed Rule. No 7(a) lenders commented on costs, though several CDCs submitted comments on increased program costs. SBA anticipates the 504 program changes will have minimal impacts on costs to CDCs, including increased costs in the program for corporate governance, reporting or increased insurance, but may also result in an increase in the CDC's processing and servicing fee income. SBA anticipates no impact on small entities as a result of grandfather clauses in the final rule. Twenty-eight (28) or 11% of CDCs expressed a concern under 120.823(e) about the increased cost of insurance as proposed. SBA concurs with the CDC comments that portfolio size should be considered and SBA should develop a sliding scale for insurance costs. SBA will coordinate with CDCs and their representatives and insurance underwriters when establishing the insurance scale, which will be presented in the next update to SOP 50 10 after the Final Rule is effective. Due to the increase in the 504 debenture size to \$5.5 million for energy public policy and manufacturing projects, SBA



proposed increasing the insurance requirements for all CDCs. A large CDC did not anticipate an increase in cost, due to its current insurance level. Currently, only those CDCs that are in the Accredited Lenders Program (ALP) have been required to have insurance of up to \$1 million. For FY 12, there were an estimated 85 ALP CDCs, or 33%, that are insured and 175 non-ALP CDCs, or 67%, which are not currently required to have insurance by SBA. SBA estimates that the changes to the eligibility requirements may increase the number of 504 loans a CDC processes and, therefore, may increase processing and servicing fee income by potentially 5–10% per CDC in the first year after the Final Rule is effective, with an overall average of a 8% rate for the national portfolio overall in the first year. As a sample, SBA reviewed the insurance and fees of a large, medium and small CDC that commented on increased insurance costs in comparison to anticipated fee income. The proportional costs of insurance as compared to the expected increase in processing and servicing fees appears to further justify a sliding scale of insurance costs based on a CDC's portfolio size.

Five, or 2% of, CDCs expressed concerns under section 120.823(d)(6) that there would be increased cost to a CDC for independent loan reviews. SBA provided clarification language to address these concerns. CDCs are not required to hire independent loan reviewers, and may comply by using independent loan reviewers who are internal to the CDC as long as they are independent of the loan approval process.

Two CDCs commented that anticipated CDC costs would increase by requiring the board to oversee investments over \$2,500. SBA addressed this concern by clarifying that this oversight is part of the CDC's budget and financial review process.

SBA received two cost comments under section 120.102, both of which referenced potential cost impacts to the SBA as a result of the elimination of the personal resources test. One comment stated this change would lower the costs to SBA. The other comment expressed a concern that costs would increase for SBA. SBA estimates this rule change will not impact the cost of program administration.

SBA received comments under sections 121.103 and 121.302 expressing concern that the proposed affidavit as to affiliation was too complicated and could result in increased costs to the borrower. As indicated above, SBA has decided to further study the affiliation

issue and is not finalizing any changes to the affiliation standards at this time.

One CDC expressed a concern about increased travel expenses due to an increase in frequency of CDC board meetings. SBA has also proposed to allow CDCs to meet via conference call and web conference to the extent permitted by State law, which should minimize compliance costs for CDCs.

One CDC expressed concern under sections 120.823(d)(12) and (d)(13) that the CDC would need to hire a consultant to develop and oversee internal controls for their CDC. One CDC expressed concern under section 120.823(d)(5) that it is cost prohibitive for smaller CDCs to provide audited financial statements. Smaller CDCs are only required to provide reviewed financial statements, not audited financial statements.

#### *Executive Order 13563*

A description of the need for this regulatory action and benefits and costs associated with this action, including possible distributional impacts that relate to Executive Order 13563, were included in the Regulatory Impact Analysis under Executive Order 12866 that was published with the proposed rule. 78 FR 12633.

SBA's two primary business loan programs operate through the agency's lending partners, which are 7(a) Lenders and CDCs. The agency has held public forums and meetings which allowed it to reach hundreds of its lending partners and gain valuable insight, guidance, and suggestions from many of them and the trade associations which represent many of them. The agency's outreach efforts to engage stakeholders before proposing this rule were extensive.

#### *Executive Order 12988*

This action meets applicable standards set forth in Sections 3(a) and 3(b)(2) of Executive Order 12988, Civil Justice Reform, to minimize litigation, eliminate ambiguity, and reduce burden. The action does not have retroactive or preemptive effect.

#### *Executive Order 13132*

SBA has determined that this final rule will not have substantial, direct effects on the States, on the relationship between the national government and the States, or on the distribution of power and responsibilities among the various levels of government. Therefore, for the purposes of Executive Order 13132, SBA has determined that this final rule has no federalism implications warranting preparation of a federalism assessment.

#### *Paperwork Reduction Act, 44 U.S.C., Ch. 35*

The SBA has determined that this final rule imposes additional reporting and recordkeeping requirements, which will result in amendments to the existing information collections identified below. SBA solicited public comments on these amendments when the proposed rule was published. SBA proposed to amend the currently approved CDC Annual Report to require CDCs to report on executive compensation and economic development projects, and to submit a copy of the CDC's tax return. The rule also proposed to require each CDC director to certify, as part of the CDC Annual Report, that he or she has read and understands the requirements set forth in 13 CFR § 120.823. Finally, SBA proposed to make changes to the governance of CDC membership; composition of CDC board of directors and to increase insurance coverage.

As a result of these new requirements, SBA has amended the following information collections:

1. *Title and Description of Information Collection:* The Certified Development Company (CDC) Annual Report Guide (SBA Form 1253) provides instructions to assist the CDC in preparing and submitting its Annual Report, which provides information to SBA on economic development, and the CDC's financial condition, operations and employment impact. *OMB Control Number:* 3245–0074.

*Description of and Estimated Number of Respondents:* All CDCs must provide an annual report. Currently there are approximately 260 CDCs. There is 1 report per respondent. The burden estimate takes into consideration the fact that respondents keep the information requested in the ordinary course of business.

*Estimated Number of Responses:* 260.

*Estimated Time per Response:* SBA estimates the time needed to complete this collection will average 28 hours per report.

*Total Estimated Hour Burden:* 260 × 28 hours = 7,280 total annual burden hours. This is 168 hours less than the current OMB inventory (7,488) as there are fewer CDCs than the last burden hour estimate for this collection.

Since proposing changes to these information collections, SBA has revised SOP 50 10, one of the Standard Operating Procedures (SOP) governing the 7(a) and 504 loan programs. Some of the amendments to the SOP will result in additional changes to SBA Forms 1919 and 1920, SBA Form 1244, and SBA Form 1253 and will result in the



elimination of SBA Forms 4, 4-I and Form 4 Schedule A. The SOP changes do not affect SBA Forms 2233 and 2234. SBA published notice in the **Federal Register** soliciting public comments on these SOP-related changes. See, 78 FR 53816 (August 30, 2013) and 78 FR 54362 (September 3, 2013); no comments were received from the public on the changes brought about by the revised SOP. SBA has submitted the forms, as revised to reflect the SOP changes, to OMB for review and approval, and will make them available on the Agency's Web site at [www.sba.gov](http://www.sba.gov) soon after obtaining OMB's approval. After this final rule becomes effective, SBA will repost the forms as revised to conform to changes made by this final rule.

*Regulatory Flexibility Act, 5 U.S.C. 601–612*

When an agency issues a rulemaking, the Regulatory Flexibility Act (RFA), 5 U.S.C. 601–612, requires the agency to “prepare and make available for public comment a final regulatory analysis” which will “describe the impact of the final rule on small entities.” Section 605 of the RFA allows an agency to certify a rule, in lieu of preparing an analysis, if the rulemaking is not expected to have a significant economic impact on a substantial number of small entities. Although the rulemaking will impact all of the approximately 4,500 7(a) Lenders (some of which are small) and all of the approximately 260 CDCs (all of which are small), SBA does not believe the impact will be significant. The grandfathering clauses in the final rule will not have an impact on small entities. As provided previously in the cost analysis in the Regulatory Impact Analysis (RIA), CDCs provided comments on the concern on increased costs in insurance, board travel for meetings and independent loan reviews. No 7(a) lenders comments on increased costs. Information about the economic impact of this rulemaking can be found in the RIA. As stated above, the final rule will expand access to the business loan program but this will not increase the burden of the agency's lending partners because they choose their own level of program participation (i.e., 7(a) Lenders and CDCs are not required to process more loan applications simply because more small businesses are eligible to apply for a business loan). For those CDCs and lenders that process more businesses loans, the benefit of the increase in revenue will far exceed any increased burden. In addition, the elimination of certain program participation requirements would not have a substantial economic impact or

cost on the small business borrower, lender or CDC.

In addition, in response to the comments that expressed concerns about increased costs in insurance, SBA will develop a sliding scale for insurance coverage to address CDC concerns of increased insurance coverage to mitigate the potential of increased costs. To address the concerns about the increased costs of board travel for meetings and independent loan reviews, SBA's final rule has provisions for web-conference and teleconference meetings that would mitigate CDCs costs of board meeting traveling to meetings. CDCs are not required to hire independent loan reviewers outside the CDC, as the independent loan review may be internal to the CDC as long as the reviewer is independent of the loan approval process. These changes should mitigate any increase in costs that may be associated with this rulemaking.

SBA believes that this final rule is SBA's best available means for facilitating American job preservation and creation by removing unnecessary regulatory requirements. Since the main purpose of this final rule is to reduce unnecessary regulatory burdens and program eligibility criteria, a review of the preamble sections above will provide additional detailed explanations regarding how and why this final rule reduces regulatory burdens and responsibly increase program participation flexibility. For these reasons, SBA has determined that there is no significant impact on a substantial number of small entities.

**List of Subjects in 13 CFR part 120**

Community development, Equal employment opportunity, Loan programs—business, Reporting and recordkeeping requirements, Small business.

For the reasons stated in the preamble, SBA amends 13 CFR part 120 as follows:

**PART 120—BUSINESS LOANS**

■ 1. The authority for 13 CFR part 120 continues to read as follows:

**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 697(a) and (e); Pub. L. 111–5, 123 Stat. 115, Pub. L. 111–240, 124 Stat. 2504.

§ 120.102 [Removed]

■ 2. Remove § 120.102.

§ 120.820 [Redesignated as § 120.816]

■ 3. Redesignate § 120.820 as § 120.816.

■ 4. Add § 120.818 to read as follows:

**§ 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.

■ 5. Add new § 120.820 to read as follows:

**§ 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.

§ 120.822 [Removed]

■ 6. Remove § 120.822.

■ 7. Revise § 120.823 to read 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 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) A CDC may not permit more than one of its Directors to be employed by or serve on the Board of Directors of any other single entity (including the entity's affiliates), unless that entity is a civic, charitable, or comparable organization that is not involved in financial services or economic development activities. No CDC Board

member may serve on the Board of another CDC in accordance with § 120.851(b).

(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 from the membership (if any), shareholders or the Board;
    - (B) Have a quorum of at least five (5) committee members authorized to vote;
    - (C) Have at least two members with commercial lending experience satisfactory to SBA; and

(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 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.

■ 8. Amend § 120.830 by revising paragraph (a) to read as follows:

**§ 120.830 Reports a CDC must submit.**

\* \* \* \* \*

(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.

\* \* \* \* \*

■ 9. Amend § 120.835 by revising paragraph (c) to read as follows:

**§ 120.835 Application to expand an Area of Operations.**

\* \* \* \* \*

(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.

**§ 120.852 [Removed and Reserved]**

■ 10. Remove and reserve § 120.852.

■ 11. Amend § 120.882 by revising paragraph (a) to read as follows:

**§ 120.882 Eligible Project costs for 504 loans.**

\* \* \* \* \*

(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;

\* \* \* \* \*

■ 12. Amend § 120.920 by revising paragraph (b) to read as follows:

**§ 120.920 Required participation by Third Party Lender.**

\* \* \* \* \*

(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.

**§ 120.925 [Removed and Reserved]**

■ 13. Remove and reserve § 120.925.

Marianne O'Brien Markowitz,  
Acting Administrator.

[FR Doc. 2014-06237 Filed 3-20-14; 8:45 am]

BILLING CODE 8025-01-P

**DEPARTMENT OF TRANSPORTATION**

**Federal Aviation Administration**

**14 CFR Part 39**

[Docket No. FAA-2013-0796; Directorate Identifier 2013-NM-111-AD; Amendment 39-17802; AD 2014-05-30]

RIN 2120-AA64

**Airworthiness Directives; The Boeing Company Airplanes**

**AGENCY:** Federal Aviation Administration (FAA), DOT.

**ACTION:** Final rule.

**SUMMARY:** We are superseding Airworthiness Directive (AD) 2013-07-07 for all The Boeing Company Model 737-600, -700, -700C, -800, -900, and -900ER series airplanes. AD 2013-07-07 required inspecting to determine the part number of the attach pins of the horizontal stabilizer rear spar, and replacing certain attach pins. This new AD clarifies the parts installation limitation and prohibition, and adds a new requirement for certain airplanes on which certain attach pins were installed. This AD was prompted by inquiries from affected operators regarding the parts installation limitation and prohibition, and re-installation of certain attach pins that were removed for inspection. We are issuing this AD to prevent premature failure of the attach pins, which could cause reduced structural integrity of the horizontal stabilizer to fuselage attachment, resulting in loss of control of the airplane.

**DATES:** This AD is effective April 25, 2014.

The Director of the Federal Register approved the incorporation by reference of a certain publication listed in this AD as of May 20, 2013 (78 FR 22182, April 15, 2013).

**ADDRESSES:** For service information identified in this AD, contact Boeing