SMALL BUSINESS ADMINISTRATION

13 CFR Part 108

RIN 3245–AE40

New Markets Venture Capital Program

AGENCY: U.S. Small Business Administration.

ACTION: Proposed rule; Proposed withdrawal of interim final rule.

SUMMARY: The U.S. Small Business Administration (''SBA'') is proposing to add a new Part 108 to implement the New Markets Venture Capital Program Act of 2000 (''the Act''). The Act authorizes SBA to issue regulations necessary to implement the program. The regulations set forth the requirements for: newly-formed venture capital companies to qualify to become New Markets Venture Capital (''NMVC'') companies to make developmental venture capital investments in smaller enterprises located in low-income geographic areas and provide operational assistance to such enterprises receiving such investments; and (2) existing Specialized Small Business Investment Companies (''SSBICs'') to qualify for grants to provide operational assistance to smaller enterprises located in low-income geographic areas and which such SSBICs have financed or expect to finance.

In today's **Federal Register**, SBA publishes an extension of the effective date of the interim final rule SBA published in the **Federal Register** on January 22, 2001, 66 FR 7218, to June 22, 2001. SBA proposes to withdraw that interim final rule before it becomes effective. SBA further proposes to implement the NMVC program instead with this proposed rule. SBA intends to complete its rulemaking and publish a final rule based on this proposed rule, before the extended effective date of the interim final rule and with sufficient time to implement the NMVC program during fiscal year 2001.

The proposed regulations in this proposed rule are based in large part on the regulations previously published in the interim final rule, with several technical and substantive changes. The **SUPPLEMENTARY INFORMATION** section of this proposed rule includes a discussion of these technical and substantive changes as well as of the comments SBA received on the interim final rule.

DATES: Submit comments on or before May 4, 2001.

ADDRESSES: Written comments should be sent to Austin Belton, Investment Division, Office of New Markets Venture Capital, U.S. Small Business Administration, 409 3rd Street, SW, Washington, DC 20416.

FOR FURTHER INFORMATION CONTACT: Austin Belton, Director, Office of New Markets Venture Capital, 202–205–7027.

SUPPLEMENTARY INFORMATION:

I. Background

The New Markets Venture Capital Program Act of 2000 (''the Act'') was created by the Consolidated Appropriations Act of 2001, Public Law 106–554, enacted December 21, 2000. Congress recognized that despite the nation's overall economic prosperity, many underserved areas in America have not experienced such prosperity and millions of Americans living in these areas do not have access to jobs or entrepreneurial opportunities. It enacted the New Markets Venture Capital (''NMVC'') Program to help create an economic infrastructure in such underserved areas by encouraging business growth through program-supported investment. This type of investing is known in the community development venture capital industry as ''double bottomline'' investing, because the investments have both an anticipated financial and social return. Social returns include creating sustainable jobs at businesses receiving investments from NMVC companies, and encouraging such businesses to provide much-needed new products and services within underserved areas.

Congress noted that between 1997 and 1998, the median income for the nation's households rose 3.5 percent in real terms, yet 12.7 percent of Americans (34.5 million people) still live below the poverty line. Many of these Americans live in inner city and rural areas, where job opportunities are scarce and there is little to attract small business investors. In rural and urban communities, poverty remains a persistent problem. Job growth is well below the national average, with unemployment at or above 14 percent. Unemployment is 7.5 percent in the African American urban community, and is 6.4 percent in the Hispanic urban population; both are nearly double the national average. Despite these statistics, Congress found that it is not enough to create jobs in these pockets of poverty, rather these communities need a new economic infrastructure to enable them to develop their full potential and participate fully in the economic mainstream. The NMVC program will encourage the growth of such an infrastructure by supporting new equity capital investments by NMVC companies and SSBICs and by providing operational assistance to smaller enterprises located in low-income geographic areas whose growth will foster the creation of wealth and job opportunities in such areas.

SBA will enter into participation agreements with NMVC companies to fulfill these statutory purposes. The Act authorizes SBA to guarantee debentures of NMVC companies. Such debentures leverage the private capital that NMVC companies must raise and enable them to make the equity investments in low-income geographic areas contemplated by the Act. The Act also authorizes SBA to provide grants to NMVC companies to provide operational assistance to smaller enterprises in which they invest. In addition, the Act enhances the ability of existing SSBICs to invest in smaller enterprises in low-income areas by giving them grants to provide operational assistance to such enterprises in connection with such investments.

SBA intends to enter into participation agreements with NMVC companies that have a solid business plan for making investments in the low-income geographic areas targeted by the Act, and that have the most likelihood of expanding economic opportunities in such areas.

II. Proposal to Withdraw Interim Final Rule

SBA published an interim final rule in the **Federal Register** on January 22, 2001, 66 FR 7218, with an effective date of February 21, 2001. SBA subsequently published in the **Federal Register** on February 20, 2001, 66 FR 10811, a delay of the effective date of the final rule until April 23, 2001. The delay was for the purpose of giving Administration officials the opportunity for further review and consideration of new regulations, consistent with the Assistant to the President and Chief of Staff memorandum entitled ''Regulatory Review Plan,'' published in the **Federal Register** on January 24, 2001. In today's **Federal Register**, SBA publishes a notice of a further extension of the effective date of the interim final rule, to June 22, 2001. The purpose of this additional extension is to give Administration officials additional time for further review and consideration of new regulations, consistent with that ''Regulatory Review Plan,'' before the interim final rule becomes effective.

SBA now proposes to withdraw that interim final rule before it becomes effective and to implement the NMVC program instead with this proposed rule. SBA seeks comments from interested members of the public on this proposed rulemaking action.

This proposed rule incorporates substantive changes resulting from the Administration's review of the interim final rule. SBA intends to complete its rulemaking and publish a final rule based on this proposed rule, before the extended effective date of the interim final rule.

SBA has published an extension of the application filing deadline, from April 19, 2001 to May 21, 2001, 66 FR 18993 (April 12, 2001). SBA hopes to be able to complete its rulemaking on this proposed rule and publish a final rule with an effective date sufficiently in advance of that date to allow potential applicants to consider the final rule and its applicability to their applications before they submit them to SBA. If SBA is unable to complete its rulemaking within that time frame, SBA may make a further extension of the application filing date so as to allow at least one week between the effective date of the final rule and the application filing deadline.

III. Discussion of Comments on Interim Final Rule

SBA received three comment letters on the interim final rule published in the **Federal Register** on January 22, 2001, 66 FR 7218. This proposed rule reflects several technical changes that are based on SBA's consideration of specific comments in those comment letters. SBA discusses those particular changes in Part B of Section III, ''Section by Section Analysis.'' In this section, SBA will discuss other significant comments recommending changes that SBA considered but chose not to include in this proposed rule.

One commenter recommended that SBA include in the definition of ''Lending Institution'' in § 108.50 any entity certified by the U.S. Department of Treasury to be a Community Development Financial Institution (''CDFI''). SBA proposes not to implement this suggestion. Many CDFIs already may qualify as ''Lending Institutions'' within the existing definition and, therefore, would not need this change to the regulation. SBA's definition of ''Lending Institution'' includes entities that are subject to regulatory oversight by third parties or other objective means of oversight, which reduces the potential for conflicts of interest with associated entities, including NMVC companies. Entities that are CDFIs can include venture capital funds and non-profit certified development companies, which may not be subject to objective oversight. Those entities associated with a NMVC company that qualify as CDFIs but not ''Lending Institutions'' within SBA's definition, may present potential conflicts of interest between those associates and the NMVC company, which justifies the requirement in proposed § 108.730(d) for prior approval by SBA of a financing with such associates.

One commenter recommended that SBA change one aspect of its management and ownership diversity regulation, § 108.150(b), to allow for a more than 70% drop-down NMVC company subject to SBA prior approval. SBA proposes not to change the 70% limitation because SBA believes that a 70% limitation on ownership of a NMVC company by one person or affiliated group of persons is reasonable, regardless of the identity or motivations of such person or persons. In addition, SBA proposes to delete language that would have allowed SBA to approve an exception to this requirement.

One commenter suggested that SBA expand the scope of the requirement for a market analysis that applicants for NMVC company designation must include in their comprehensive business plans, § 108.320(c). Specifically, the commenter requested that SBA add to the end of the first sentence in that subsection the phrase '' * * * and the low-income individuals living in those areas.'' SBA proposes not to implement this suggestion, for two reasons.

First, this would add a requirement on applicants that goes beyond the scope of the Act. ''Low-income individual'' is a defined term in section 351(2) of the Small Business Investment Act (''SBI Act''), as amended by the Act. The Act uses that defined term only in the context of the Administrator's discretionary ability to designate additional areas as LI areas (see section 351(3)(A)(iii) of the SBI Act as amended by the Act). Section 352(1) of the SBI Act, as amended by the Act, describes one of the purposes of the NMVC program as promoting economic development in LI areas and ''among individuals living in such areas.'' Congress could have used the defined term ''low-income individuals'' here, if it had so intended, but chose not to. Therefore, SBA believes it would be going beyond the statutory language and purpose to impose a requirement on NMVC company applicants to demonstrate how its activities will have a positive economic impact on the ''low-income individuals living in'' LI areas.

Second, the market analysis requirement in this section already requires applicants to analyze how its activities will have a positive economic impact on the LI areas in which it intends to focus its activities. SBA intends that applicants include in this analysis a discussion of all relevant aspects of economic impact on the LI areas, which reasonably would include impact on residents of the areas.

One commenter stated that it believes SBA did not include in § 108.360, which addresses criteria for conditional approval, certain elements the commenter believes the Act requires SBA to consider in selecting NMVC company applicants for conditional approval.

Section 354(c)(2) of the SBI Act, as amended by the Act, sets forth the criteria SBA must consider in selecting NMVC company applicants for conditional approval. Section 354(c)(2)(E) requires SBA to consider the likelihood that an applicant will be able to satisfy the conditions set forth in section 354(d) of the SBI Act, as amended by the Act. Sections 354(d)(1) and (2) set forth the minimum amounts of capital and grant matching resources a conditionally approved NMVC company must raise in order to be considered for final approval. Proposed § 108.360 sets forth the evaluation criteria SBA proposes to consider in selecting applicants for participation in the NMVC program. One of those criteria, proposed § 108.360(h), is the likelihood and the time frame within which the applicant will be able to raise the minimum amounts of capital and grant matching resources the company must raise in order to be considered for final approval.

SBA believes that this adequately implements the statutory requirement in section 354(c)(2)(E) that SBA consider the likelihood that an applicant will be able to raise the resources required under section 354(d) within the required time period. In addition, in the competitive selection process for participation in the NMVC program, SBA intends to evaluate each applicant's plan for raising required resources and the likelihood that the applicant can implement its plan.

One commenter suggested that SBA revise § 108.380(a)(1)(i)(B) to limit the amount of grant matching resources a conditionally approved NMVC company must raise in order to receive final approval. The commenter suggested this limit should be an amount not more than the amount of operational assistance grant that SBA has ''conditionally designated for that NMVC company.'' SBA proposes not to implement this suggestion for several reasons.

First, SBA will not ''conditionally designate'' or otherwise commit or obligate its appropriated funds for operational assistance grants to conditionally approved NMVC

companies and SSBIC grant applicants. SBA will obligate its appropriated funds only to finally approved NMVC companies and SSBICs that raise the required amounts of capital and grant matching resources by the applicable deadlines.

Second, the statutory scheme created by the Act provides that conditionally approved NMVC companies must raise at least a specified minimum of capital and grant matching resources by a deadline established by SBA. There is no prohibition on a conditionally approved NMVC company raising more capital than it proposed to raise in the plan it submitted to SBA and upon which SBA gave conditional approval. If a conditionally approved NMVC company did so, however, pursuant to the Act it also must raise additional grant matching resources in an amount not less than 30 percent of the capital it actually raised. In addition, there also is no statutory prohibition on a NMVC company raising the minimum of $5 million in capital but raising more than the minimum amount for grant matching resources of 30% of capital. If one or more conditionally approved NMVC companies raised more grant matching resources than anticipated at the time of selections for conditional approval, that could result in SBA not having sufficient appropriated funds to make grants equal to the full amount of each NMVC company's grant matching resources. In that event, SBA would have to use the pro rata reduction provision in proposed § 108.2020(c).

One commenter believes that the regulations do not, but should, require a NMVC company to provide reports to SBA concerning small businesses that receive operational assistance but not financing from the NMVC company or small businesses in which the NMVC company invests (''portfolio concerns'') that are located outside LI areas. Specifically, the commenter states that section 361(2) of the SBI Act, as amended by the Act, requires a NMVC company to report the number and percentage of employees of such businesses that reside in LI areas. Another commenter suggested that SBA expand the scope of the reporting requirements set forth in § 108.630(e) to include required reporting on the full-time equivalent jobs created and the percentage of these jobs filled by people who were low-income individuals immediately prior to employment in such jobs. SBA proposes not to implement this second suggestion because SBA believes this goes beyond the scope and purpose of the Act. See discussion, above, concerning ''low-income individual.''

Proposed § 108.630(e) already addresses the first suggestion, because it would require a NMVC company to report to SBA certain social, economic, or community development impact information concerning every financing the NMVC company makes. SBA has developed a reporting form specifically for this purpose (SBA Form 468, Schedule 9). This reporting requirement applies to both low-income investments and to any other financing the NMVC company makes (including financings the NMVC company makes in businesses located outside LI areas). NMVC companies must provide information concerning each of its portfolio concerns, on the number of the concern's full-time employees that reside both inside and outside the LI areas and the quality of those jobs (for example, whether health insurance and pension plan benefits are provided). With respect to a small business to which the NMVC company provides operational assistance but not also a financing, SBA proposes to implement the other part of the first suggestion, by requiring a NMVC company to report on the numbers of that small business' employees that reside inside and outside of a LI area. This reporting requirement will be contained within the grant award agreement between SBA and finally approved NMVC companies.

One commenter recommended that SBA reduce or eliminate the examination fee set forth in § 108.692. SBA considered the suggestion but proposes not to implement it. The examination fee for NMVC companies is comparable to or lower than the examination fee for a similarly-sized SBIC. SBA expects the examination of NMVC companies to be significantly more complex than the examination required for SBICs. For example, SBA will be required to audit a NMVC company's reporting on the economic, social, and community impact of its financings, and its use of operational assistance funds.

One commenter suggested that SBA ease the requirement in § 108.710 that 80 percent of the businesses receiving financing from a NMVC company must be low-income enterprises (defined in proposed § 108.50 as smaller enterprises located in LI areas at the time the financing is made) and must receive equity capital investments, in order to give NMVC companies more investing flexibility. The commenter recommends a revision that would allow the 80 percent of businesses that must be low-income enterprises to not necessarily be the same 80 percent of businesses that receive equity capital investments.

SBA proposes not to implement this suggestion. SBA believes the clear statutory purpose behind the NMVC program, as set forth in sections 352(1) and (2) of the SBI Act, as amended by the Act, is specifically to address the unmet equity needs of smaller enterprises located in LI areas, not generally the unmet credit needs of such businesses. By requiring the same 80% of smaller enterprises located in LI areas also to receive equity capital investments, this statutory purpose is better served.

One commenter suggested that it might be impossible for a NMVC company to comply with the requirements of § 108.710(a) if, at the end of the NMVC company's fiscal year, it has invested most or all of its capital and is unable to draw leverage in order to make additional investments to bring itself into compliance. This comment anticipates that a NMVC company will use all of its private capital first, before drawing any leverage. SBA does not anticipate this problem will arise for a NMVC company that is properly using both its regulatory capital and leverage to make investments. SBA expects NMVC companies to utilize the debenture leverage available under the NMVC program as they make investments.

One commenter suggested that SBA eliminate the prohibition in § 108.800(b) that a NMVC company may not provide a credit guarantee for an unincorporated portfolio company. SBA proposes not to implement this suggestion. This is a long-standing policy in the SBIC program and SBA believes it also should be applicable to NMVC companies.

IV. Section by Section Analysis

This section by section analysis is divided into two parts. Part A includes a description of each proposed regulation. Part B describes each regulation for which SBA proposes a significantly changed version from the version of that regulation that was published in the interim final rule, and the basis for the change. These changes include technical and substantive changes.

A. Section by Section Analysis of Regulations

The following is a section by section analysis of SBA's proposed rule to add a new part 108 to title 13 of the Code of Federal Regulations to implement the Act.

1. General Information About the Regulations

As you read through the section by section analysis of particular

regulations, you will see that we propose to model many of these regulations on similar regulations governing SBA's Small Business Investment Company (''SBIC'') program, found in part 107 of this title. In addressing the challenge of implementing the NMVC program, SBA is able to draw upon the experience that it has gained over the last 43 years in administering the SBIC program.

The SBIC program was created by the Small Business Investment Act of 1958 in response to a Federal Reserve study finding that small businesses in general were unable to obtain the long-term debt and equity funds that they needed for success. The basic objective of the program is to attract and supplement private capital, managed by private investment managers, to meet that need. SBA licenses such companies as SBICs, regulates their activities to ensure that they are financially sound and serve the program's public policy objectives, and supplements their private capital by guaranteeing debentures or other securities that they issue.

The SBIC program has been extraordinarily successful in recent years and today represents a major factor in small business financing. It is estimated that 34 percent of all companies receiving institutional venture capital in 1999 obtained it from an SBIC. In fiscal year 2000, SBICs invested a record $5.5 billion in more than 3,000 small growth companies. This was accomplished with a budget appropriation of just $24.3 million.

A key strength of the SBIC program lies in the fact that all investment decisions are made by private individuals with their own money at first risk. However, this also represents a limitation in that such investment activities are profit driven and generally are not targeted to small businesses located in low-income areas. Low-income investments typically are smaller and more costly to make, and they require significantly more assistance over the investment period than most SBIC investments. At the same time, they generally offer a more limited profit potential to the investor. The NMVC program addresses these factors by adding to the SBIC structure an operational assistance grant subsidy and by recruiting managers and investors that have an economic development objective in addition to their financial one.

Because of these many similarities between SBICs and NMVC companies and between these two venture capital programs, SBA proposes to incorporate into the NMVC program many of the SBIC regulations that SBA believes are fundamental to the safety and soundness of the SBIC program.

2. Section by Section Analysis

Proposed §§ 108.10 through 108.50 briefly describe the NMVC program, state the legal basis for the program, definitions, and provide guidance on how to read part 108. Most of the definitions come directly from part 107 of this title, which governs the SBIC program. Most of the newly defined terms come directly from the Act, and SBA proposes not to supplement or modify them. SBA also proposes several new definitions, including terms ''Low-Income Enterprise'' and ''Low-Income Investment'' as a shorter way to describe equity capital investments in a smaller enterprise that, at the time of the initial financing, has its principal office located in a low-income geographic area.

Proposed §§ 108.100 through 108.160 describe the qualifications for the NMVC program. Under the Act, NMVC companies must be newly-formed, for-profit entities. SBA proposes to require that NMVC companies be organized under state law and be either corporations, limited liability companies, or limited partnerships. SBA proposes to require that they have qualified management, have economic development as their primary mission, and identify particular low-income geographic areas in which they propose to focus their investment activities. SBA models these regulations on the SBIC program, including the requirements that NMVC companies must have management and ownership diversity and that SBA will require pre-approval of all management expenses of a NMVC company (see §§ 107.100 through 107.160 of this title).

Proposed §§ 108.200 through 108.240 address capitalization of a NMVC company, including minimum capital requirements, permitted sources of capital, and limitations on non-cash contributions to capital. These regulations also are modeled on similar regulations in the SBIC program (see §§ 107.200 through 107.250 of this title).

Proposed §§ 108.300 through 108.330 set forth policies and procedures for application for designation as a NMVC company. SBA proposes to allow submission of applications for participation in the NMVC program only during a specific application period, to be set forth in a Notice of Funds Availability subsequently published in the **Federal Register**, as opposed to a rolling admissions process. SBA proposes to use this method of selecting applicants for three reasons. One reason is that SBA believes this method will enable SBA to achieve the statutory directive of ensuring, to the extent possible and given the applications received, nationwide availability of developmental venture capital. SBA proposes to compare applications both for quality and other criteria described in the regulations, and for the geographic areas they intend to cover so as to choose the best applications for each geographic area and avoid duplication within specific geographic areas. Another reason is that SBA has received one-year appropriated funds for operational assistance grants, and the statute requires SBA to distribute available appropriated funds pro rata among NMVC companies and SSBICs that apply for such grants. (See discussion of §§ 108.2000 through 108.2040 for more information about how SBA proposes to administer the operational assistance grant program.) Submission of all applications for these grant funds at the same time will allow SBA to distribute these funds among all eligible and qualified recipients. Third, SBA believes this procedure will allow SBA to orderly administer appropriated funds it may receive in subsequent fiscal years, by allowing SBA to open up the NMVC program to new rounds of applicants.

SBA proposes to require applicants for participation in the NMVC program to submit an application, similar to the application for the SBIC program but which also includes the requirement for a comprehensive business plan. Many of the topics SBA proposes to require applicants to include in their business plans are outlined in section 354(b) of the SBI Act, as amended by the Act, regarding application for the NMVC program. In addition, SBA proposes to use the following additional topics: market analysis of the specific low-income areas towards which the applicant proposes to target its investments and other activities, operational capacity and investment strategies, plans for raising capital and matching funds for operational assistance grants, and projected amount of investment in low-income areas as opposed to outside those areas. Based in part on the experience of other Federal agencies with similar economic development programs, SBA believes these additional topics will allow SBA to ensure that applicants understand the objectives of the NMVC program and have a good plan for accomplishing those objectives and for creating and maintaining a viable investment fund.

SBA also proposes to assess a fee for receiving a grant under the NMVC program to ensure that applicants are

professional venture capital firms committed to participate in the program.

Proposed §§ 108.340 through 108.395 describe SBA's evaluation criteria and selection process for participation in the NMVC program. SBA proposes to consider ten criteria in its evaluation and selection of applicants for participation in the NVMC program. Most of the specified criteria are set forth in the Act. SBA proposes to use the following additional selection criteria not specifically described in the Act: the quality of the applicant's business plan in terms of meeting the objectives of the program; the strength and likelihood for success of the applicant's operations and investment strategies; the need for developmental venture capital investments in the geographic areas in which the applicant proposes to concentrate its activities; and the extent of the applicant's understanding of the markets in such geographic areas. Based in part on the experience of other Federal agencies with similar economic development programs, SBA believes these additional evaluation criteria are effective indicators of whether the objectives of the NMVC program will be met.

The Act provides for SBA to conditionally approve companies for participation in the NMVC program, based on SBA's evaluation of their applications. Conditionally approved companies must raise the required amounts of capital and of matching funds for the operational assistance grant award from SBA within a time period specified by SBA. As provided in the Act, SBA will finally approve as NMVC companies all conditionally approved NMVC companies that raise the required amount of capital within the time period specified by SBA and sign a participation agreement with SBA. Proposed § 108.380(b) also sets forth procedures under which SBA may grant to conditionally approved companies, as provided in the Act, an exception to the requirement to raise all of their required matching funds for their operational assistance grants before SBA designates them as finally approved NMVC companies.

Proposed §§ 108.400 through 108.470 describe SBA's requirements for changes in ownership, control, or structure of a NMVC company. These regulations are modeled after similar regulations for the SBIC program (see §§ 107.400 through 107.475 of this title).

Proposed §§ 108.500 through 108.585 describe SBA's requirements for managing the operations of a NMVC company. These regulations are modeled after similar regulations for the SBIC program (see §§ 107.500 through 107.590 of this title).

Proposed §§ 108.600 through 108.680 describe SBA's record keeping, record retention, and reporting requirements for NMVC companies. These regulations are modeled after similar regulations for the SBIC program (see §§ 107.600 through 107.680 of this title). SBA also proposes to require each NMVC company to provide reports concerning the community development impact of each investment it makes, as well as reports on its administration and use of grant funds as required by Circular A–110 of the Office of Management and Budget, ''Uniform Administrative Requirements for Grants and Agreements with Institutions of Higher Education, Hospitals, and other Non-Profit Organizations.'' SBA anticipates that to the extent not inconsistent with SBA's regulations for the NMVC program, NMVC companies' administration and use of grant funds will be subject to OMB Circular A–110 and to Part 31 of the Federal Acquisition Regulations, 48 CFR 31.000 *et seq.*, ''Contract Cost Principles and Procedures.'' OMB Circular A–110 is optional for use in connection with grants to commercial organizations. SBA proposes to apply it to NMVC companies in order to take advantage of existing and well-known grant administrative procedures and policies to facilitate SBA's orderly administration of grants to NMVC companies. (See the discussion of §§ 108.2000 through 108.2040 concerning applicability of these same procedures and policies to grants to SSBICs.)

Proposed §§ 108.690 through 108.692 describe SBA's requirements for SBA's examinations of NMVC companies. These regulations are modeled after similar regulations for the SBIC program (see §§ 107.690 through 107.692 of this title).

Proposed §§ 108.700 through 108.885 describe SBA's requirements for determining the eligibility of financings of small businesses by NMVC companies, and regarding types of allowable financings. These regulations are modeled after similar regulations for the SBIC program (see §§ 107.700 through 107.885 of this title).

Proposed § 108.710 sets forth the requirement that at the close of each year, 80 percent of the concerns that NMVC companies have financed must be smaller enterprises that, as of the time of the initial financing, had their principal office in a low-income geographic area and in which the NMVC companies have made equity capital investments as defined in the regulations (see proposed § 108.50). This regulation implements the requirement outlined in the definition of ''participation agreement'' in section 351(6)(B) of the SBI Act. SBA interprets this statutory section to refer to 80 percent of the businesses in which a NMVC company invests.

Proposed §§ 108.1100 through 108.1720 describe SBA's requirements and procedures for NMVC companies to obtain leverage from SBA and the procedures governing how SBA will fund leverage. These regulations are modeled after similar regulations for the SBIC program (see §§ 107.1100 through 107.1720 of this title).

Proposed §§ 108.1810 through 108.1840 describe defaults by NMVC companies on the terms and conditions governing their participation in the NMVC program, and SBA's remedies upon such defaults. These regulations are modeled after similar regulations for the SBIC program (see §§ 107.1810 through 107.1840 of this title).

Proposed § 108.1900 concerns termination by a NMVC company of its participation in the NMVC program. This regulation is modeled after a similar regulation for the SBIC program (see § 107.1900 of this title).

Proposed §§ 108.1910 through 108.1930 address miscellaneous issues, including application for an exemption from regulatory requirements and the effect of regulation changes on transactions previously consummated. These regulations are modeled after similar regulations for the SBIC program (see §§ 107.1910 through 107.1930 of this title).

Proposed § 108.1940 sets forth procedures under which SBA may designate additional census tracts or equivalent county divisions as low-income geographic areas. This regulation implements the authority given to SBA's Administrator in section 351(3)(A)(iii) of the SBI Act, as amended by the SBI Act. SBA has designed these procedures to allow for maximum opportunity by interested members of the public to ask SBA to designate specific census tracts or equivalent county divisions as additional low-income geographic areas.

Proposed §§ 108.2000 through 108.2040 set forth requirements and procedures for operational assistance grants to both NMVC companies and to SSBICs. SBA proposes to award such grants only after receiving and evaluating applications in response to a Notice of Funds Availability published in the **Federal Register**. SBA proposes to award grants to SSBICs and to NMVC companies in such a way as to promote developmental venture capital

investments nationwide and in both urban and rural areas.

SBA also proposes to require SSBICs to provide reports on its administration and use of grant funds as required by Circular A–110 of the Office of Management and Budget, ''Uniform Administrative Requirements for Grants and Agreements with Institutions of Higher Education, Hospitals, and other Non-Profit Organizations.'' SBA anticipates that to the extent not inconsistent with these regulations, SSBICs' administration and use of grant funds will be subject to OMB Circular A–110 and to part 31 of the Federal Acquisition Regulations, 48 CFR 31.000 *et seq.*, ''Contract Cost Principles and Procedures.'' OMB Circular A–110 is optional for use in connection with grants to commercial organizations. SBA proposes to apply it to SSBICs in order to take advantage of existing and well-known grant administrative procedures and policies to facilitate SBA's orderly administration of grants to SSBICs.

B. Discussion of Changes to Regulations as Published in Interim Final Rule

SBA wishes to help members of the public who already are familiar with the version of the regulations published as an interim final rule to focus only on those changes SBA makes in this proposed rule to that original version of the regulations. Accordingly, in this Part B SBA describes only those regulations to which SBA made significant changes and the basis for the changes.

In § 108.50, SBA proposes to change the previously published version of the definitions of Equity Capital Investment, Financing or Financed, and Trust Certificate Rate to make technical corrections. SBA proposes to change the previously published version of the definition of Relevant Venture Capital Finance to eliminate reference to intent and instead focus on demonstrable prior actions, and to further distinguish this definition from the definition of Community Development Finance. The proposed definition of Community Development Finance focuses on any type of financing (debt or equity) in low-income communities. The definition also does not limit the relevant experience in terms of the types of entities receiving the financing. By contrast, the proposed, revised definition of Relevant Venture Capital Finance focuses more specifically on equity-type investments in small businesses in low-income communities or benefiting low-income communities. SBA believes that this change will better enable an applicant for NMVC company designation to demonstrate in its application the relevant types of experience.

SBA proposes to change the previously published version of § 108.110 to add the word ''team'' in the first sentence. The purpose of this change is to clarify that the management team as a whole, as opposed to each member of the team individually, must have knowledge, experience and capability in Community Development Finance or Relevant Venture Capital Finance satisfactory to SBA.

SBA proposes to change the previously published version of § 108.240 by withdrawing it in its entirety because, upon SBA's further consideration, SBA believes it will not be necessary or desirable for NMVC companies to have the ability to include non-cash contributions in Private Capital. SBA also proposes to make technical changes to the previously published version of §§ 108.200 and 108.230(d) to reflect the withdrawal of § 108.240.

SBA proposes to change the previously published version of § 108.320 by revising paragraphs (f) and (g). This section addresses the contents of the comprehensive business plan that applicants for NMVC company designation must submit for SBA's consideration. Paragraph (f) concerns the applicant's plan for providing operational assistance. One commenter expressed concern that the regulations did not clearly require NMVC companies to use licensed professionals, when necessary, to provide operational assistance to small business. Section 354(c)(2)(G) of the SBI Act, as amended by the Act, requires SBA to evaluate, among other things, the strength of an applicant's proposal to provide operational assistance to small business concerns, ''as the proposal relates to * * * the use of resources for the services of licensed professionals, when necessary * * *'' The previously published version of paragraph (f) in § 108.320 stated that applicants must address whether and to what extent they plan to use licensed professionals, which leaves open the possibility that they might choose not to use licensed professionals. In order to clarify that NMVC companies selected by SBA must use licensed professionals, when necessary, SBA proposes to revise paragraph (f) to require applicants to address how they plan to use licensed professionals, when necessary. SBA also proposes to revise the previously published version of § 108.2000(b)(4)(ii)(A) to make the same change with respect to an SSBIC applicant's planned use of operational assistance grant funds.

Another commenter suggested that SBA revise this paragraph (f) to request that in addition to addressing when applicants plan to use licensed professionals, they also address how they plan to provide operational assistance through the use of their own staff versus outside entities. SBA considers that applicants necessarily will have to address this topic in their plan for providing operational assistance and, therefore, believes that this topic need not be set forth as a specific requirement.

SBA also proposes to revise the previously published version of paragraph (g) to make a technical change suggested by a commenter.

SBA proposes to change the previously published version of § 108.330 to revise the name of the fee and when it is due. SBA reconsidered the provisions in the Act that authorize SBA to charge fees, and has determined that SBA has authority to charge a fee in connection with SBA's issuance of a grant. SBA proposes to require applicants for NMVC company designation, who will be entitled to a grant upon final approval as a NMVC company, to pay this fee in advance at the time of application submission. This will ensure that applicants are professional venture capital firms committed to participate in the program. However, SBA proposes to revise the previously published version of the regulation to state that SBA will refund this fee to those applicants that SBA does not select for conditional approval or final approval. SBA also proposes to revise the previously published version of the regulation to require payment of the full fee in advance, to reduce SBA's administrative costs to deposit fees and issue refunds.

SBA proposes to change the previously published version of § 108.340 by inserting the phrase ''(if any)'' in the first sentence to clarify that SBA may or may not conduct interviews or site visits with NMVC company applicants, depending on available time and resources. SBA proposes that only if SBA does in fact conduct such interviews or site visits will SBA consider them in evaluating and selecting applicants for conditional approval.

SBA proposes to change the previously published version of § 108.520 to clarify that SBA must approve both the initial management expenses of a NMVC company, and any subsequent increase in such expenses.

SBA proposes to change the previously published version of § 108.710 to add a new substantive requirement. The previously published

version of the regulation required that at the end of each fiscal year, 80 percent of a NMVC company's portfolio concerns must be low-income enterprises and must receive equity capital investments. In other words, 80 percent of the business concerns receiving financing must have received an equity capital investment, be a smaller enterprise, and be located in a low-income geographic area (''LI area''). SBA proposes that in addition, for all financings extended by a NMVC company, the NMVC company must have invested at least 80 percent (in total dollars) in low-income investments. In other words, 80 percent of the dollars used to finance business concerns must be invested in equity capital investments in smaller enterprises located in LI areas.

This additional provision would require that most of a NMVC company's capital and leverage go toward making equity investments in smaller enterprises located in LI areas. SBA believes that this will fulfill one of the Act's purposes—to address the unmet equity investment needs of businesses located in LI areas. SBA has not required 100 percent of a NMVC company's capital and leverage to meet this requirement, however, in order to give a NMVC company some flexibility as to its use of the remaining 20 percent. A NMVC company may choose to make other kinds of investments with a lower risk and/or higher anticipated rate of return to offset the expectation of higher risk and lower rate of return from low-income investments, in order to ensure the overall economic viability of the NMVC company. The economic viability of a NMVC company is an important public policy consideration because it better ensures both the safety and soundness of the use of taxpayer dollars for leverage and grant assistance to NMVC companies and the ability of a NMVC company to attract private investment dollars.

SBA proposes to change the previously published version of § 108.720 by revising paragraphs (b)(2) and (h). The previously published version of paragraph (b)(2) would be revised to require that a NMVC company must obtain SBA's prior written approval before financing a passive small business. SBA believes that this issue will not arise with any frequency, considering the types and sizes of financings NMVC companies are likely to make. However, to the extent that it does arise, by requiring advance approval SBA intends to ensure narrow application of this exception to the rule that only active operating small business concerns are eligible to receive financing from a NMVC company.

SBA also proposes to change the previously published version of paragraph (h) to include an additional situation in which a small business is ineligible for financing. SBA proposes that a NMVC company would be prohibited from providing funds that a small business will use to purchase stock in or provide capital to a Small Business Investment Company (''SBIC'') or to repay indebtedness incurred for the purpose of investing in an SBIC.

SBA proposes to change the previously published version of § 108.1230 to make technical corrections. In paragraph (d)(3), which addresses which representatives of a NMVC company from whom SBA will accept a certification in connection with a draw of leverage, SBA proposes to add to the list an individual who is authorized to act as or for a member-manager. This change addresses NMVC companies that are organized as limited liability companies. Similarly, SBA proposes to change the previously published version of § 108.1810 to make a technical correction, to address NMVC companies that are organized as limited liability companies.

SBA proposes to make several changes to the previously published version of § 108.2000. SBA proposes to change paragraph (b)(3) to charge a $5,000 grant issuance fee to SSBICs applying for grants under the NMVC program. SBA proposes that this fee will be in the same amount as that charged to applicants for the NMVC company program and will be refunded in full if the SSBIC does not receive a grant award. This change is necessary to treat all applicants for operational assistance grants under the NMVC program the same.

SBA also proposes to change the previously published version of § 108.2000(b)(4)(ii), which describes the elements of the plan an SSBIC must submit to SBA as part of its application for an operational assistance grant. SBA proposes to add four new issues that an SSBIC's plan must address: track record of management team in obtaining public policy results through investments; market analysis; regulatory capital; and projected impact. These changes are necessary to treat all applicants for operational assistance grants under the NMVC program the same.

SBA also proposes to change the previously published version of § 108.2000(b)(5), which describes the evaluation and selection criteria SBA will use to select SSBICs for an operational assistance grant. SBA proposes to add six new criteria in subparagraphs (ii), (iv), (v), (vi), (vii), and (viii). These changes are necessary to treat all applicants for operational assistance grants under the NMVC program the same.

SBA proposes to change the previously published version of § 108.2030 to revise the allowable time period within which binding commitments or annuities for grant matching resources may be payable to a NMVC company or SSBIC. SBA proposes that the allowable time period be five years. The reason for this change is that both Federal funds and matching resources must be available and expended within the same time period. By law, SBA's grant funds will be available for expenditure from the date of award to a date not more than five years from that date. As a result, the time period within which the grantee's grant matching resources are available to the grantee must not exceed the time period within which SBA grant funds will be available.

V. Regulatory Compliance Section—Compliance With Executive Orders 12866, 12988 and 13132, and the Paperwork Reduction Act (44 U.S.C. Ch. 35)

Compliance With Executive Order 12866

The Office of Management and Budget (OMB) has reviewed this proposed rule as a ''significant'' regulatory action under Executive Order 12866. A regulatory assessment is set forth below.

Low-income communities in the United States face multiple and varied barriers to sustainable growth. But a common obstacle for virtually all such communities is that they are unable to attract sufficient equity capital and technical assistance for starting and expanding businesses. Federal Reserve Board Chair Alan Greenspan has observed that equity capital is crucial to the existence of an innovative and productive business community, especially in lower-income communities. Yet the existing private venture-capital industry is heavily concentrated in affluent, high technology regions located in only a handful of states.

In order to promote economic development and address the unmet equity needs of smaller businesses located in low-income areas, Congress passed and President Clinton signed into law the legislation creating the NMVC program. SBA proposes to use these regulations to implement and administer the NMVC program. NMVC companies will be newly formed, for-profit investment companies with

private management. Their objective will be to create an economic infrastructure in underserved areas. NMVC companies will accomplish this by making equity investments in smaller enterprises, primarily located in low-income geographic areas. SBA anticipates that this type of investing will generate both financial and social returns. The social returns can include creating sustainable jobs at businesses receiving investments from NMVC companies, and encouraging such businesses to provide much-needed new products and services within underserved areas.

SBA estimates that the NMVC program will cost approximately $1 million annually to administer. The cost to the government includes the costs of staff (including benefits) and all other overhead expenses. SBA proposes to select participants for the NMVC program and regulate NMVC operations to ensure that public policy objectives are being met. Toward that end, SBA proposes to require NMVC companies to provide regular performance reports and take part in annual financial examinations.

SBA estimates that it will cost a NMVC company approximately $6,000 to apply for designation as a NMVC company, not including a $5,000 grant issuance fee due in advance at the time of application. This includes the cost of one staff person at a level comparable to a Federal employee at a GS–13 grade level spending 160 hours to complete the application. After receiving designation as a NMVC company, the annual cost to the NMVC company will be based on compliance with the reporting requirements of the program. SBA anticipates that compliance with the reporting requirements of the program will cost approximately $1,500. This includes the cost of one staff person at a level comparable to a Federal employee at a GS–13 grade level spending approximately 40 hours preparing the required performance and financial reports. The costs to NMVC companies and SSBICs that choose to participate in the grant aspect of the program include approximately $1,500 to prepare the initial grant application (approximately 40 hours of work), and approximately $600 annually thereafter to prepare the required quarterly status reports (approximately 16 hours of work). Again, these costs are estimated based upon one staff person at a level comparable to a Federal employee at a GS–13 grade level. There is also a fee payable by the NMVC company each time SBA examines the company. This rulemaking action proposes a base fee for the examination of $3,500.

SBA believes that there are no alternatives to the planned regulatory action that could more adequately address the equity needs of the nation's low-income areas. In developing the regulations, application package and reporting materials SBA purposefully followed proven industry practices. Based upon the foregoing, SBA believes that its proposed rule implements the congressionally-mandated NMVC program in the most cost effective and efficient manner.

Compliance With Executive Order 12988

SBA certifies that this proposed rule is drafted, to the extent practicable, in accordance with the standards set forth in section 3 of Executive Order 12988.

Compliance With Executive Order 13132

For purposes of Executive Order 13132, SBA has determined that this proposed rule has no federalism implications because the legislation authorizing it addresses private, for-profit concerns (NMVC companies) working directly with entrepreneurs.

Compliance With Paperwork Reduction Act, 44 U.S.C. Ch. 35.

For purposes of the Paperwork Reduction Act, 44 U.S.C. Ch. 35, the collection of information (''collection'') for this program includes the NMVC program application package and reporting and recordkeeping requirements. SBA previously requested from the Office of Management and Budget (''OMB'') an emergency clearance of this collection. OMB reviewed and approved the collection and assigned OMB control number 3245–0332.

SBA has made the collection available to the public on SBA's web site at http://www.sba.gov/inv and by calling Terri Dennin at (202) 205–6234. SBA already has provided the public with a 60-day comment period on this collection (66 FR 7218). SBA received no comments on the collection.

List of Subjects in 13 CFR Part 108

Community development, Government securities, Grant programs—business, Securities, Small businesses.

For the reasons stated in the preamble, the Small Business Administration is proposing to add 13 CFR part 108 as follows:

PART 108—NEW MARKETS VENTURE CAPITAL (''NMVC'') PROGRAM

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Authority: 15 U.S.C. 634(b)(6) and Pub. L. 106–544 (114 Stat. 2763).

Subpart A—Introduction to Part 108

§ 108.10 Description of the New Markets Venture Capital Program.

The New Markets Venture Capital (''NMVC'') Program is a developmental venture capital program for the purpose of promoting economic development and the creation of wealth and job

opportunities in low-income geographic areas and among individuals living in such areas. SBA selects and then enters into participation agreements with selected newly formed venture capital companies, and provides leverage in the form of debenture guarantees to such companies to allow them to make equity capital investments in smaller enterprises located in low-income geographic areas. SBA also awards grants to such companies and to Specialized Small Business Investment Companies so that they can provide operational assistance to such smaller enterprises in connection with such investments.

§ 108.20 Legal basis and applicability of this part 108.

The regulations in this part implement Part B of Title III of the Small Business Investment Act of 1958, as amended. All NMVC Companies must comply with all applicable SBA regulations, accounting guidelines and valuation guidelines for NMVC Companies, available from SBA.

§ 108.30 Amendments to Act and regulations.

A NMVC Company is subject to all existing and future provisions of the Act and parts 108 and 112 of title 13 of the Code of Federal Regulations.

§ 108.40 How to read this part 108.

(a) *Center headings.* All references in this part to SBA forms, and instructions for their preparation, are to the current issue of such forms. Center headings are descriptive and are used for convenience only. They have no regulatory effect.

(b) *Capitalizing defined terms.* Terms defined in § 108.50 have initial capitalization in this part 108.

(c) *''You.''* The pronoun ''you'' as used in this part 108 means a NMVC Company unless otherwise noted.

Subpart B—Definition of Terms Used in Part 108

§ 108.50 Definition of terms.

Act means the Small Business Investment Act of 1958, as amended.

Affiliate or *Affiliates* has the meaning set forth in § 121.103 of this chapter.

Applicant means any entity submitting an application to SBA for designation as a NMVC Company under this part.

Articles mean articles of incorporation or charter for a Corporate NMVC Company, the partnership agreement or certificate for a Partnership NMVC Company, and the operating agreement or other organizational documents for a LLC NMVC Company.

Assistance or *Assisted* means Financing of or management services rendered to a Small Business by or through a NMVC Company pursuant to the Act and the regulations in this part.

Associate of a NMVC Company means any of the following:

(1)(i) An officer, director, employee or agent of a Corporate NMVC Company;

(ii) A Control Person, employee or agent of a Partnership NMVC Company;

(iii) A managing member of a LLC NMVC Company;

(iv) An Investment Adviser/Manager of any NMVC Company, including any Person who contracts with a Control Person of a Partnership NMVC Company to be the Investment Adviser/Manager of such NMVC Company; or

(v) Any Person regularly serving a NMVC Company on retainer in the capacity of attorney at law.

(2) Any Person who owns or controls, or who has entered into an agreement to own or control, directly or indirectly, at least 10 percent of any class of stock of a Corporate NMVC Company or 10 percent of the membership interests of an LLC NMVC Company, or a limited partner's interest of at least 10 percent of the partnership capital of a Partnership NMVC Company. However, neither a limited partner in a Partnership NMVC Company nor a non-managing member in an LLC NMVC Company is considered an Associate if such Person is an entity Institutional Investor whose investment in the Partnership, including commitments, represents no more than 33 percent of the capital of the NMVC Company and no more than five percent of such Person's net worth.

(3) Any officer, director, partner (other than a limited partner), manager, agent, or employee of any Associate described in paragraph (1) or (2) of this definition.

(4) Any Person that directly or indirectly Controls, or is Controlled by, or is under Common Control with, a NMVC Company.

(5) Any Person that directly or indirectly Controls, or is Controlled by, or is under Common Control with, any Person described in paragraphs (1) and (2) of this definition.

(6) Any Close Relative of any Person described in paragraphs (1), (2), (4), and (5) of this definition.

(7) Any Secondary Relative of any Person described in paragraphs (1), (2), (4), and (5) of this definition.

(8) Any concern in which—

(i) Any person described in paragraphs (1) through (6) of this definition is an officer; general partner, or managing member; or

(ii) Any such Person(s) singly or collectively Control or own, directly or indirectly, an equity interest of at least 10 percent (excluding interests that such Person(s) own indirectly through ownership interests in the NMVC Company).

(9) Any concern in which any Person(s) described in paragraph (7) of this definition singly or collectively own (including beneficial ownership) a majority equity interest, or otherwise have Control. As used in this paragraph (9), ''collectively'' means together with any Person(s) described in paragraphs (1) though (7) of this definition.

(10) For the purposes of this definition, if any Associate relationship described in paragraphs (1) through (7) of this definition exists at any time within six months before or after the date that a NMVC Company provides Financing, then that Associate relationship is considered to exist on the date of the Financing.

(11) If any NMVC Company has any ownership interest in another NMVC Company, the two NMVC companies are Associates of each other.

Capital Impairment has the meaning set forth in § 108.1830(b).

Central Registration Agent or *CRA* means one or more agents appointed by SBA for the purpose of issuing TCs and performing the functions enumerated in § 108.1620 and performing similar functions for Debentures funded outside the pooling process.

Close Relative of an individual means:

(1) A current or former spouse;

(2) A father, mother, guardian, brother, sister, son, daughter; or

(3) A father-in-law, mother-in-law, brother-in-law, sister-in-law, son-in-law, or daughter-in-law.

Commitment means a written agreement between a NMVC Company and an eligible Small Business that obligates the NMVC Company to provide Financing (except a guarantee) to that Small Business in a fixed or determinable sum, by a fixed or determinable future date. In this context the term ''agreement'' means that there has been agreement on the principal economic terms of the Financing. The agreement may include reasonable conditions precedent to the NMVC Company's obligation to fund the commitment, but these conditions must be outside the NMVC Company's control.

Common Control means a condition where two or more Persons, either through ownership, management, contract, or otherwise, are under the Control of one group or Person. Two or more NMVC companies 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; or if they are managed or their investments are significantly directed either by a common independent investment advisor or managerial contractor, or by two or more such advisors or contractors that are Affiliates of each other. This presumption may be rebutted by evidence satisfactory to SBA.

Community Development Finance means debt and equity-type investments in low-income communities.

Conditionally Approved NMVC Company means a company that—

(1) Has applied for participation as a NMVC Company, and

(2) SBA has conditionally approved to participate in the NMVC program for a specified period of time not to exceed two years, subject to the company fulfilling the requirements to be a NMVC Company within that specified period of time.

Control means the possession, direct or indirect, of the power to direct or cause the direction of the management and policies of a NMVC Company or other concern, whether through the ownership of voting securities, by contract, or otherwise.

Control Person means any Person that controls a NMVC Company, either directly or through an intervening entity. A Control Person includes:

(1) A general partner of a Partnership NMVC Company;

(2) Any Person serving as the general partner, officer, director, or manager (in the case of a limited liability company) of any entity that controls a NMVC Company, either directly or through an intervening entity;

(3) Any Person that—

(i) Controls or owns, directly or through an intervening entity, at least 10 percent of a Partnership NMVC Company or any entity described in paragraphs (1) or (2) of this definition; and

(ii) Participates in the investment decisions of the general partner of such Partnership NMVC Company;

(4) Any Person that controls or owns, directly or through an intervening entity, at least 50 percent of a Partnership NMVC Company or any entity described in paragraphs (1) or (2) of this definition.

Corporate NMVC Company. See definition of NMVC Company in this section.

Debentures means debt obligations issued by NMVC companies pursuant to section 355 of the Act and held or guaranteed by SBA.

Debt Securities are instruments evidencing a loan with an option or any other right to acquire Equity Securities in a Small Business or its Affiliates, or a loan which by its terms is convertible into an equity position. Consideration must be paid for all options that you acquire.

Developmental Venture Capital means capital in the form of Equity Capital Investments in Smaller Enterprises made with a primary objective of fostering economic development in Low-Income Geographic Areas.

Distribution means any transfer of cash or non-cash assets to SBA, its agent or Trustee, or to partners in a Partnership NMVC Company, or to shareholders in a Corporate NMVC Company, or to members in an LLC NMVC Company. Capitalization of Retained Earnings Available for Distribution constitutes a Distribution to the NMVC Company's non-SBA partners, shareholders, or members.

Equity Capital Investments means investments in the form of common or preferred stock, limited partnership interests, options, warrants, or similar equity instruments, including subordinated debt with equity features if such debt provides only for interest payments contingent upon and limited to the extent of earnings. Equity Capital Investments must not require amortization. Equity Capital Investments may be guaranteed by one or more third parties; however, neither Equity Capital Investments nor such guarantee may be collateralized or otherwise secured. Investments classified as Debt Securities are not precluded from qualifying as Equity Capital Investments. Equity Capital Investments may provide for royalty payments only if the royalty payments are based on the earnings of the concern.

Equity Securities means stock of any class in a corporation, stock options, warrants, limited partnership interests in a limited partnership, membership interests in a limited liability company, or joint venture interests.

Financing or *Financed* means outstanding financial assistance provided to a Small Business by a NMVC Company, whether through:

(1) Loans;

(2) Debt Securities;

(3) Equity Securities;

(4) Guarantees; or

(5) Purchases of securities of a Small Business through or from an underwriter (see § 108.825).

Guaranty Agreement means the contract entered into by SBA which is a guarantee backed by the full faith and credit of the United States Government as to timely payment of principal and interest on Debentures and SBA's rights in connection with such guarantee.

Includible Non-Cash Gains means those non-cash gains (as reported on SBA Form 468) that are realized in the form of Publicly Traded and Marketable securities or investment grade debt instruments. For purposes of this definition, investment grade debt instruments means those instruments that are rated ''BBB'' or ''Baa'', or better, by Standard & Poor's Corporation or Moody's Investors Service, respectively. Non-rated debt may be considered to be investment grade if a NMVC Company obtains a written opinion from an investment banking firm acceptable to SBA stating that the non-rated debt instrument is equivalent in risk to the issuer's investment grade debt.

Institutional Investor means:

(1) *Entities.* Any of the following entities if the entity has a net worth (exclusive of unfunded commitments from investors) of at least $1 million, or such higher amount as is specified in this paragraph (1). (See also § 108.230(c)(4) for limitations on the amount of an Institutional Investor's commitment that may be included in Private Capital.)

(i) A State or National bank, trust company, savings bank, or savings and loan association.

(ii) An insurance company.

(iii) A 1940 Act Investment Company or Business Development Company (each as defined in the Investment Company Act of 1940, as amended (15 U.S.C. 8a–1 *et seq.*).

(iv) A holding company of any entity described in paragraph (l)(i), (ii) or (iii) of this definition.

(v) An employee benefit or pension plan established for the benefit of employees of the Federal government, any State or political subdivision of a State, or any agency or instrumentality of such government unit.

(vi) An employee benefit or pension plan (as defined in the Employee Retirement Income Security Act of 1974, as amended (Pub. L. 93–406, 88 Stat. 829), excluding plans established under section 401(k) of the Internal Revenue Code of 1986 (26 U.S.C. 401(k)), as amended).

(vii) A trust, foundation or endowment exempt from Federal income taxation under the Internal Revenue Code of 1986, as amended.

(viii) A corporation, partnership or other entity with a net worth (exclusive of unfunded commitments from investors) of more than $10 million.

(ix) A State, a political subdivision of a State, or an agency or instrumentality of a State or its political subdivision.

(x) An entity whose primary purpose is to manage and invest non-Federal funds on behalf of at least three Institutional Investors described in paragraphs (l)(i) through (l)(ix) of this definition, each of whom must have at least a 10 percent ownership interest in the entity.

(xi) Any other entity that SBA determines to be an Institutional Investor.

(2) *Individuals.* (i) Any of the following individuals if he/she is also a permanent resident of the United States:

(A) An individual who is an Accredited Investor (as defined in the Securities Act of 1933, as amended (15 U.S.C. 77a-77aa)) and whose commitment to the NMVC Company is backed by a letter of credit from a State or National bank acceptable to SBA.

(B) An individual whose personal net worth is at least $2 million and at least ten times the amount of his or her commitment to the NMVC Company. The individual's personal net worth must not include the value of any equity in his or her most valuable residence.

(C) An individual whose personal net worth, not including the value of any equity in his or her most valuable residence, is at least $10 million.

(ii) Any individual who is not a permanent resident of the United States but who otherwise satisfies paragraph (2)(i) of this definition provided such individual has irrevocably appointed an agent within the United States for the service of process.

Investment Adviser/Manager means any Person who furnishes advice or assistance with respect to operations of a NMVC Company under a written contract executed in accordance with the provisions of § 108.510.

Lending Institution means a concern that is operating under regulations of a state or Federal licensing, supervising, or examining body, or whose shares are publicly traded and listed on a recognized stock exchange or NASDAQ and which has assets in excess of $500 million; and which, in either case, holds itself out to the public as engaged in the making of commercial and industrial loans and whose lending operations are not for the purpose of financing its own or an Associate's sales or business operations.

Leverage means financial assistance provided to a NMVC Company by SBA through the guaranty of a NMVC Company's Debentures, and any other SBA financial assistance evidenced by a security of the NMVC Company.

Leverageable Capital means Regulatory Capital, excluding unfunded commitments.

LLC NMVC Company. See definition of NMVC Company in this section.

Loan means a transaction evidenced by a debt instrument with no provision for you to acquire Equity Securities.

Loans and Investments means Portfolio securities, assets acquired in liquidation of Portfolio securities, operating concerns acquired, and notes and other securities received, as set forth in the Statement of Financial Position of SBA Form 468.

Low-Income Enterprise means a Smaller Enterprise that, as of the time of the initial Financing, has its Principal Office located in a Low-Income Geographic Area.

Low-Income Geographic Area (''LI Area'') means—

(1) Any population census tract (or in the case of an area that is not tracted for population census tracts, the equivalent county division, as defined by the Bureau of the Census of the United States Department of Commerce for purposes of defining poverty areas), if—

(i) The poverty rate for that census tract is not less than 20 percent;

(ii) In the case of a tract—

(A) That is located within a metropolitan area, 50 percent or more of the households in that census tract have an income equal to less than 60 percent of the area median gross income; or

(B) That is not located within a metropolitan area, the median household income for such tract does not exceed 80 percent of the statewide median household income; or

(C) As determined by the Administrator in accordance with § 108.1940 of this part, a substantial population of Low-Income Individuals reside, an inadequate access to investment capital exists, or other indications of economic distress exist in that census tract; or

(2) any area located within—

(i) A Historically Underutilized Business Zone (''HUBZone'') as defined in section 3(p) of the Small Business Act and 13 CFR 126.103;

(ii) An Urban Empowerment Zone or Urban Enterprise Community (as designated by the Secretary of the United States Department of Housing and Urban Development); or

(iii) A Rural Empowerment Zone or Rural Enterprise Community (as designated by the Secretary of the United States Department of Agriculture).

Low-Income Individual means an individual whose income (adjusted for family size) does not exceed—

(1) For metropolitan areas, 80 percent of the area median income; and

(2) For nonmetropolitan areas, the greater of—

(i) 80 percent of the area median income, or

(ii) 80 percent of the statewide nonmetropolitan area median income.

Low-Income Investment means an Equity Capital Investment in a Low-Income Enterprise.

Management Expenses has the meaning set forth in § 108.520.

NAICS Manual means the latest issue of the North American Industrial Classification System Manual, prepared by the Office of Management and Budget, and available from the U.S. Government Printing Office, Superintendent of Documents, P.O. Box 371954, Pittsburgh, Pa., 15250–7954.

New Markets Tax Credit program means the tax credit created by the Consolidated Appropriations Act of 2001, Pub L. No. 106–554, enacted December 21, 2000, to be implemented by the Internal Revenue Service, United States Department of Treasury.

New Markets Venture Capital Company or *NMVC Company* means a corporation (Corporate NMVC Company), a limited partnership organized as required by § 108.160 (Partnership NMVC Company), or a limited liability company (LLC NMVC Company) that—

(1) Has been granted final approval by SBA under § 108.390 of this part, and

(2) Has entered into a Participation Agreement with SBA. For certain purposes, the Entity General Partner of a Partnership NMVC Company is treated as if it were a NMVC Company (see § 108.160(a)).

1940 Act Company means a NMVC Company which is registered under the Investment Company Act of 1940.

1980 Act Company means a NMVC Company which is registered under the Small Business Investment Incentive Act of 1980.

Operational Assistance means management, marketing, and other technical assistance that assists a Small Business with its business development.

Original Issue Price means the price paid by the purchaser for securities at the time of issuance.

Participation Agreement means an agreement between SBA and a company to which SBA has granted final approval under § 108.390 of this part, that—

(1) Details the company's operating plan and investment criteria; and

(2) Requires the company to make investments in Smaller Enterprises at least 80 percent of which Smaller Enterprises are located in LI Areas.

Partnership NMVC Company. See definition of NMVC Company in this section.

Person means a natural person or legal entity.

Pool means an aggregation of SBA guaranteed Debentures approved by SBA.

Portfolio means the securities representing a NMVC Company's total outstanding Financing of Smaller Enterprises. It does not include idle funds or assets acquired in liquidation of Portfolio securities.

Portfolio Concern means a Small Business Assisted by a NMVC Company.

Principal Office means the location where the greatest number of the concern's employees at any one location perform their work. However, for those concerns whose ''primary industry'' (see 13 CFR 121.107) is service or construction (see 13 CFR 121.201), the determination of principal office excludes the concern's employees who perform the majority of their work at job-site locations to fulfill specific contract obligations.

Private Capital has the meaning set forth in § 108.230.

Publicly Traded and Marketable means securities that are salable without restriction or that are salable within 12 months pursuant to Rule 144 (17 CFR 230.144) of the Securities Act of 1933, as amended, by the holder thereof, and are of a class which is traded on a regulated stock exchange, or is listed in the Automated Quotation System of the National Association of Securities Dealers (NASDAQ), or has, at a minimum, at least two market makers as defined in the relevant sections of the Securities Exchange Act of 1934, as amended (15 U.S.C. 77b *et seq.*), and in all cases the quantity of which can be sold over a reasonable period of time without having an adverse impact upon the price of the stock.

Regulatory Capital means:

(1) *General.* Regulatory Capital means Private Capital, excluding non-cash assets contributed to a NMVC Company, a Conditionally Approved NMVC Company, or an Applicant, and non-cash assets purchased by a Conditionally Approved NMVC Company or an Applicant, unless such assets have been converted to cash or have been approved by SBA for inclusion in Regulatory Capital. For purposes of this definition, sales of contributed non-cash assets with recourse or borrowing against such assets shall not constitute a conversion to cash.

(2) *Exclusion of questionable commitments.* An investor's commitment to a NMVC Company, Conditionally Approved NMVC Company, or Applicant is excluded from Regulatory Capital if SBA determines that the collectability of the commitment is questionable.

(3) *Exclusion of amounts designated for Operational Assistance match.* Regulatory Capital excludes any portion of Private Capital that is designated as matching resources in accordance with § 108.2030(b)(3).

Relevant Venture Capital Finance means Equity Capital Investments in small businesses in low-income communities or benefiting low-income communities.

Retained Earnings Available for Distribution means Undistributed Net Realized Earnings less any Unrealized Depreciation on Loans and Investments (as reported on SBA Form 468), and represents the amount that a NMVC Company may distribute to investors (including SBA) as a profit Distribution, or transfer to Private Capital.

SBA means the Small Business Administration, 409 Third Street, SW., Washington, DC 20416.

Secondary Relative of an individual means:

(1) A grandparent, grandchild, or any other ancestor or lineal descendent who is not a Close Relative;

(2) An uncle, aunt, nephew, niece, or first cousin; or

(3) A spouse of any person described in paragraph (1) or (2) of this definition.

Small Business means a small business concern as defined in section 103(5) of the Act (including its Affiliates), and which meets the criteria applicable to the Small Business Investment Company program as set forth in part 121 of this chapter.

Small Business Investment Company (SBIC) means a Licensee, as that term is defined in § 107.50 of this chapter.

Smaller Enterprise means any Small Business that:

(1) Together with its Affiliates has a net worth of not more than $6.0 million and average net income after Federal income taxes (excluding any carry-over losses) for the preceding two years no greater than $2.0 million, or

(2) Both together with its Affiliates, and by itself, meets the size standard of § 121.201 of this title at the time of Financing for the industry in which it is then primarily engaged.

Specialized Small Business Investment Companies (SSBICs) means any Small Business Investment Company that—

(1) Invests solely in small business concerns that contribute to a well-balanced national economy by facilitating ownership in such concerns by persons whose participation in the free enterprise system is hampered because of social or economic disadvantages; and

(2) Was licensed under section 301(d) of the Small Business Investment Act, as in effect before September 30, 1996.

Trust means the legal entity created for the purpose of holding guaranteed Debentures and the guaranty agreement related thereto, receiving, holding and making any related payments, and accounting for such payments.

Trust Certificate Rate means a fixed rate determined at the time Debentures are pooled.

Trust Certificates (TCs) means certificates issued by SBA, its agent or Trustee and representing ownership of all or a fractional part of a Trust or Pool of Debentures.

Trustee means the trustee or trustees of a Trust.

Undistributed Net Realized Earnings means Undistributed Realized Earnings less Non-cash Gains/Income, each as reported on SBA Form 468.

Unrealized Appreciation means the amount by which a NMVC Company's valuation of each of its Loans and Investments, as determined by its Board of Directors or General Partner(s) in accordance with NMVC Company's valuation policies, exceeds the cost basis thereof.

Unrealized Depreciation means the amount by which a NMVC Company's valuation of each of its Loans and Investments, as determined by its Board of Directors or General Partner(s) in accordance with NMVC Company's valuation policies, is below the cost basis thereof.

Unrealized Gain (Loss) on Securities Held means the sum of the Unrealized Appreciation and Unrealized Depreciation on all of a NMVC Company's Loans and Investments, less estimated future income tax expense or estimated realizable future income tax benefit, as appropriate.

Subpart C—Qualifications for the NMVC Program

Organizing a NMVC Company

§ 108.100 Business form.

A NMVC Company must be a newly formed for-profit entity or, subject to § 108.150, a newly formed for-profit subsidiary of an existing entity. It must be organized under State law solely for the purpose of performing the functions and conducting the activities contemplated under the Act. It may be organized as a corporation (''Corporate NMVC Company''), a limited partnership (''Partnership NMVC Company''), or a limited liability company (''LLC NMVC Company'').

§ 108.110 Qualified management.

An Applicant must show, to the satisfaction of SBA, that its current or proposed management team is qualified and has the knowledge, experience, and capability in Community Development Finance or Relevant Venture Capital Finance, necessary for investing in the types of businesses contemplated by the Act, these regulations and its business plan. In determining whether an Applicant's current or proposed management team has sufficient qualifications, SBA will consider information provided by the Applicant and third parties concerning the background, capability, education, training and reputation of its general partners, managers, officers, key personnel, and investment committee and governing board members. The Applicant must designate at least one individual as the official responsible for contact with SBA.

§ 108.120 Economic development primary mission.

The primary mission of a NMVC Company must be economic development of one or more LI Areas.

§ 108.130 Identified low income geographic areas.

A NMVC Company must identify the specific LI Areas in which it intends to make Developmental Venture Capital investments and provide Operational Assistance under the NMVC program.

§ 108.140 SBA approval of initial management expenses.

A NMVC Company must have its Management Expenses approved by SBA at the time of designation as a NMVC Company. (See § 108.520 for the definition of Management Expenses.)

§ 108.150 Management and ownership diversity requirement.

(a) *Diversity requirement.* You must have diversity between management and ownership in order to be a NMVC Company. To establish diversity, you must meet the requirements in paragraphs (b) and (c) of this section.

(b) *Percentage ownership requirement.* No Person or group of Persons who are Affiliates of one another may own or control, directly or indirectly, more than 70 percent of your Regulatory Capital or your Leverageable Capital.

(c) *Non-affiliation requirement.* At least 30 percent of your Regulatory Capital and Leverageable Capital must be owned and controlled by Persons unaffiliated with your management and unaffiliated with each other, and whose investments are significant in dollar and percentage terms as determined by SBA. Such Persons must not be your Associates (except for their status as your shareholders, limited partners or members) and must not Control, be Controlled by, or be under Common Control with any of your Associates. A single ''acceptable'' Institutional Investor may be substituted for two or three of the three investors who are otherwise required. The following Institutional Investors are ''acceptable'' for this purpose:

(1) Entities whose overall activities are regulated and periodically examined by state, Federal or other governmental authorities satisfactory to SBA;

(2) Entities listed on the New York Stock Exchange;

(3) Entities that are publicly-traded and that meet both the minimum numerical listing standards and the corporate governance listing standards of the New York Stock Exchange:

(4) Public or private employee pension funds;

(5) Trusts, foundations, or endowments, but only if exempt from Federal income taxation; and

(6) Other Institutional Investors satisfactory to SBA.

(d) *Voting requirement.* The investors required for you to satisfy diversity may not delegate their voting rights to any Person who is your Associate, or who Controls, is Controlled by, or is under Common Control with any of your Associates, without prior SBA approval.

(e) *Requirement to maintain diversity.* You must maintain management-ownership diversity while you are a NMVC Company. If, at any time, you no longer have the required management-ownership diversity, you must:

(1) Notify SBA within 10 days; and

(2) Re-establish diversity within six months.

§ 108.160 Special rules for NMVC Companies formed as limited partnerships.

(a) *Entity General Partner.* (1) A general partner which is a corporation, limited liability company or partnership (an ''Entity General Partner'') shall be organized under state law solely for the purpose of serving as the general partner of one or more NMVC companies.

(2) SBA must approve any person who will serve as an officer, director, manager, or general partner of the Entity General Partner. This provision must be stated in an Entity General Partner's Certificate of Incorporation, operating agreement, limited partnership agreement or other similar governing instrument.

(3) An Entity General Partner is subject to the same examination and reporting requirements as a NMVC Company under sections 361 and 362 of the Act. The restrictions and obligations imposed upon a NMVC Company by §§ 108.1810, 108.30, 108.410 through 108.450, 108.470, 108.500, 108.510, 108.585, 108.600, 108.680, 108.690 through 108.692, and 108.1910 apply also to an Entity General Partner of a NMVC Company.

(4) The general partner(s) of your Entity General Partner(s) will be considered your general partner.

(5) If your Entity General Partner is a limited partnership, its limited partners may be considered your Control Person(s) if they meet the definition for Control Person in § 108.50.

(b) *Other requirements for Partnership NMVC Companies.* If you are a Partnership NMVC Company:

(1) You must have a minimum duration of 10 years or two years following the maturity of your last-maturing Leverage security, whichever is longer. After 10 years, if all Leverage has been repaid or redeemed and all amounts due SBA, its agent, or Trustee have been paid, the Partnership NMVC Company may be terminated by a vote of your partners;

(2) None of your general partner(s) may be removed or replaced by your limited partners without prior written approval of SBA;

(3) Any transferee of, or successor in interest to, your general partner shall have only the rights and liabilities of a limited partner pending SBA's written approval of such transfer or succession; and

(4) You must incorporate all the provisions in this paragraph (b) in your limited partnership agreement.

(c) *Obligations of a Control Person.* All Control Persons are bound by the disciplinary provisions of sections 365 and 366 of the Act and by the conflict-of-interest rules under § 108.730. The term NMVC Company, as used in §§ 108.30, 108.460, and 108.680, includes all of the NMVC Company's Control Persons. The conditions specified in § 108.1810 and § 108.1910 apply to all general partners.

(d) *Liability of general partner for partnership debts to SBA.* Subject to section 365 of the Act, your general partner is not liable solely by reason of its status as a general partner for repayment of any Leverage or debts you owe to SBA unless SBA, in the exercise of reasonable investment prudence, and with regard to your financial soundness, determines otherwise prior to the purchase or guaranty of your Leverage.

(e) *Special Leverage requirement.* Before your first issuance of Leverage, you must furnish SBA with evidence that you qualify as a partnership for tax purposes, either by a ruling from the

Internal Revenue Service or by an opinion of counsel.

Capitalizing a NMVC Company

§ 108.200 Adequate capital for NMVC Companies.

You must meet the requirements of these §§ 108.200 through 108.230 in order to qualify for designation as a NMVC Company and to receive Leverage.

§ 108.210 Minimum capital requirements for NMVC Companies.

You must have Regulatory Capital of at least $5,000,000 and Leverageable Capital of at least $500,000 to become a NMVC Company.

§ 108.230 Private Capital for NMVC Companies.

(a) *General.* Private Capital means the contributed capital of a NMVC Company, plus unfunded binding commitments by Institutional Investors (including commitments evidenced by a promissory note) to contribute capital to a NMVC Company.

(b) *Contributed capital.* For purposes of this section, contributed capital means the paid-in capital and paid-in surplus of a Corporate NMVC Company, the members' contributed capital of a LLC NMVC Company, or the partners' contributed capital of a Partnership NMVC Company, in each case subject to the limitations in paragraph (c) of this section.

(c) *Exclusions from Private Capital.* Private Capital does not include:

(1) Funds borrowed by a NMVC Company from any source.

(2) Funds obtained through the issuance of Leverage.

(3) Funds obtained directly from any Federal agency or department.

(4) Any portion of a commitment from an Institutional Investor with a net worth of less than $10 million that exceeds 10 percent of such Institutional Investor's net worth.

(d) *Non-cash capital contributions.* Capital contributions in a form other than cash are excluded from Private Capital.

(e) *Contributions with borrowed funds.* You may not accept any capital contribution made with funds borrowed by a Person seeking to own an equity interest (whether direct or indirect, beneficial or of record) of at least 10 percent of your Private Capital. This exclusion does not apply if:

(1) Such Person's net worth is at least twice the amount borrowed; or

(2) SBA gives its prior written approval of the capital contribution.

Subpart D—Application and Approval Process for NMVC Company Designation

§ 108.300 When and how to apply for designation as a NMVC Company.

(a) *Notice of Funds Availability (''NOFA'').* SBA will publish a NOFA in the **Federal Register**, advising potential applicants of the availability of funds for the NMVC program. An entity may then submit an application for designation as a NMVC Company. When submitting its application, an Applicant must comply with both these regulations and any requirements specified in the NOFA, including submission deadlines. The NOFA may specify limitations, special rules, procedures, and restrictions for a particular funding round.

(b) *Application form.* An Applicant must apply for designation as a NMVC Company using the application packet provided by SBA. Upon receipt of an application, SBA may request clarifying or technical information on the materials submitted as part of the application.

§ 108.310 Contents of application.

Each Applicant must submit a complete application, including the following:

(a) *Amounts.* The Applicant must indicate the amounts of—

(1) Regulatory Capital it proposes to raise;

(2) Binding commitments for contributions in cash or in-kind it proposes to raise, and/or an annuity it proposes to purchase, in accordance with the requirements of § 108.2030, as its matching resources for its Operational Assistance grant award (the aggregate of which must be not less than 30 percent of the Regulatory Capital it proposes to raise under paragraph (a)(1) of this section).

(b) *Comprehensive business plan.* The Applicant must submit a comprehensive business plan covering at least a five-year period, addressing the specific items described in § 108.320, and which demonstrates that the Applicant has the capacity to operate successfully as a NMVC Company.

(c) *New Markets Tax Credit program.* Applicant must address if and to what extent it intends to conform its activities to the New Markets Tax Credit laws. If Applicant plans to seek a New Markets Tax Credit, Applicant also must state the amount of tax credit allocation it intends to seek.

§ 108.320 Contents of comprehensive business plan.

(a) *Executive summary.* The executive summary must include a description of—

(1) The Applicant;

(2) Its strategy for how it proposes to make successful Developmental Venture Capital investments in identified LI Areas;

(3) The markets in the LI Areas it proposes to serve; and

(4) How it intends to work with community organizations in and be accountable to the residents of identified LI Areas in order to facilitate its Developmental Venture Capital investments.

(b) *Capacity, skills, and experience of the management team.* An Applicant must provide information generally as to the background, capability, education, reputation and training of its general partners, managers, officers, key personnel, investment committee and governing board members. The Applicant also must provide information specifically on these individuals' qualifications and reputation in the areas of Community Development Finance and/or Relevant Venture Capital Finance, including the impact of these individuals' activities in these areas.

(c) *Market analysis.* An Applicant must provide an analysis of the LI Areas in which it intends to focus its Developmental Venture Capital investments and Operational Assistance to Smaller Enterprises, demonstrating that the Applicant understands the market and the unmet capital needs in such areas and how its activities will meet these unmet capital needs through Developmental Venture Capital investments and will have a positive economic impact on those areas. The analysis must include a description of the extent of the economic distress in the identified LI Areas. An Applicant also must analyze the extent of the demand in such areas for Developmental Venture Capital investments and any factors or trends that may affect the Applicant's ability to make effective Developmental Venture Capital investments.

(d) *Operational capacity and investment strategies.* An Applicant must submit information concerning its policies and procedures for underwriting and approving its Developmental Venture Capital investments, monitoring its portfolio, and maintaining internal controls and operations.

(e) *Regulatory Capital.* An Applicant must include a detailed description of how it plans to raise its Regulatory

Capital. An Applicant must discuss its potential sources of Regulatory Capital, the estimated timing on raising such funds, and the extent of the expressions of interest to commit such funds to the Applicant.

(f) *Plan for providing Operational Assistance.* An Applicant must describe how it plans to use its grant funds to provide Operational Assistance to Smaller Enterprises in which it will make Developmental Venture Capital investments. Its plan must address the types of Operational Assistance it proposes to provide, and how it plans to provide the Operational Assistance through the use of licensed professionals, when necessary, either from its own staff or from outside entities.

(g) *Matching resources for Operational Assistance grant.* An Applicant must include a detailed description of how it plans to obtain binding commitments for cash or in-kind contributions, and/or to purchase an annuity, to match the funds requested from SBA for the Applicant's Operational Assistance grant. If it proposes to obtain commitments for cash or in-kind contributions, it also must estimate the ratio of cash to in-kind contributions (in no event may in-kind contributions exceed 50 percent of the total contributions). Applicant must discuss its potential sources of matching resources, the estimated timing on raising such funds, and the extent of the expressions of interest to commit such funds to the Applicant. Potential sources of matching resources must satisfy the requirements in § 108.2030(b)(1).

(h) *Projected amount of investment in LI Areas.* An Applicant must describe the amount of its total Regulatory Capital and Leverage that it proposes to invest in Smaller Enterprises located in LI Areas, as compared to the amount that it proposes to invest in Small Businesses located outside of LI Areas.

(i) *Projected impact.* An Applicant must describe the criteria and economic measurements to be used to evaluate whether and to what extent it has met the objectives of the NMVC program. It must include:

(1) A description of the extent to which it will concentrate its Developmental Venture Capital investments and Operational Assistance activities in identified LI Areas;

(2) An estimate of the social, economic, and community development benefits to be created within identified LI Areas over the next five years or more as a result of its activities;

(3) A description of the criteria to be used to measure the benefits created as a result of its activities;

(4) A discussion about the amount of such benefits created that it will consider to constitute successfully meeting the objectives of the NMVC program.

(j) *Affiliates and business relationships.* Applicant must submit information regarding the management and financial strength of any parent or holding entity, affiliated firm or entity, or any other firm or entity essential to the success of the Applicant's business plan.

§ 108.330 Grant issuance fee.

An Applicant must pay to SBA a grant issuance fee of $5,000. An Applicant must submit this fee in advance, at the time of application submission. If SBA does not select an Applicant as a Conditionally Approved NMVC Company or designate an Applicant as a NMVC Company, SBA will refund this fee to the Applicant.

Subpart E—Evaluation and Selection of NMVC Companies.

§ 108.340 Evaluation and selection—general.

SBA will evaluate and select an Applicant to participate in the NMVC program solely at SBA's discretion, based on SBA's review of the Applicant's application materials, interviews or site visits with the Applicant (if any), and background investigations conducted by SBA and other Federal agencies. SBA's evaluation and selection process is intended to—

(a) Ensure that Applicants are evaluated on a competitive basis and in a fair and consistent manner;

(b) Take into consideration the unique proposals presented by Applicants;

(c) Ensure that each Applicant that SBA designates as a NMVC Company can fulfill successfully the goals of its comprehensive business plan; and

(d) Ensure that SBA selects Applicants in such a way as to promote Developmental Venture Capital investments nationwide and in both urban and rural areas.

§ 108.350 Eligibility and completeness.

SBA will not consider any application that is not complete or that is submitted by an Applicant that does not meet the eligibility criteria described in subpart C of this part. SBA, at its sole discretion, may request from an Applicant additional information concerning eligibility criteria or easily completed portions of the application in order to allow SBA to consider that Applicant's application.

§ 108.360 Evaluation criteria.

SBA will evaluate and select an Applicant for participation in the NMVC program by considering the following criteria—

(a) The quality of the Applicant's comprehensive business plan in terms of meeting the objectives of the NMVC program;

(b) The likelihood that the Applicant will fulfill the goals described in its comprehensive business plan;

(c) The capability of the Applicant's management team;

(d) The strength and likelihood for success of the Applicant's operations and investment strategies;

(e) The need for Developmental Venture Capital investments in the LI Areas in which the Applicant intends to invest;

(f) The extent to which the Applicant will concentrate its activities on serving the LI Areas in which it intends to invest, including the ratio of resources that it proposes to invest in such areas as compared to other areas;

(g) The Applicant's demonstrated understanding of the markets in the LI Areas in which it intends to focus its activities;

(h) The likelihood that and the time frame within which the Applicant will be able to—

(1) Raise the Regulatory Capital it proposes to raise for its investments, and

(2) obtain the binding commitments for contributions in cash or in-kind and/or an annuity it proposes to obtain as its matching resources for its Operational Assistance grant award;

(i) The strength of the Applicant's proposal to provide Operational Assistance to Smaller Enterprises in which it plans to invest;

(j) The extent to which the activities proposed by the Applicant will promote economic development and the creation of wealth and job opportunities in the LI Areas in which it intends to invest and among individuals living in LI Areas; and

(k) The strength of the Applicant's application compared to applications submitted by other Applicants intending to invest in the same or proximate LI Areas.

§ 108.370 Conditional approval.

From among the Applicants submitting eligible and complete applications, SBA will select a number of Applicants and will conditionally approve such selected Applicants to participate in the NMVC program. SBA

will give each such Conditionally Approved NMVC Company a specific period of time, not to exceed two years, to satisfy the requirements to become a NMVC Company.

§ 108.380 Final approval as a NMVC Company.

(a) *General rule.* With respect to each Conditionally Approved NMVC Company, SBA will either:

(1) Grant final approval to participate in the NMVC program and designate such company as a NMVC Company, if such Conditionally Approved NMVC Company:

(i) Within the specific period of time SBA gave to it when SBA conditionally approved it for participation in the NMVC program, has raised:

(A) At least $5,000,000 of Regulatory Capital; and

(B) At least $1,500,000 of matching resources for its Operational Assistance grant award or 30 percent of the Regulatory Capital it raised, whichever is greater; and

(ii) Enters into a Participation Agreement with SBA; or

(2) Revoke SBA's conditional approval of the company, at which time it is no longer a Conditionally Approved NMVC Company and must not participate in the NMVC program or represent itself as a Conditionally Approved NMVC Company.

(b) *Exception to requirement to raise matching resources*—(1) *General.* At its discretion and based upon a showing of good cause, SBA may consider a Conditionally Approved NMVC Company to have satisfied the requirement in paragraph (a)(1)(i)(B) of this section to raise matching resources in the amount of at least 30 percent of its Regulatory Capital if the Conditionally Approved NMVC Company—

(i) Already has raised at least 20 percent of the total amount of required matching resources; and

(ii) Has a viable plan that reasonably projects its capacity to raise the remainder of the required amount of matching resources.

(2) *Request for exception.* Before the expiration of the time period given to it by SBA to meet the requirements to become a NMVC Company, a Conditionally Approved NMVC Company may submit to SBA a request that SBA grant the exception described in paragraph (b)(1) of this section. Such Conditionally Approved NMVC must present to SBA evidence of good cause for such request, as well as evidence supporting the elements of the exception described in such paragraph.

(3) *No applicability to Regulatory Capital.* The exception described in this section applies only to matching resources for the Operational Assistance grant award. Under no circumstances will SBA designate a Conditionally Approved NMVC Company as a NMVC Company if such Conditionally Approved NMVC Company does not raise the required minimum amount of Regulatory Capital within the time period SBA gave it to do so.

Subpart F—Changes in Ownership, Structure, or Control

Changes in Control or Ownership of NMVC Company

§ 108.400 Changes in ownership of 10 percent or more of NMVC Company but no change of Control.

You must obtain SBA's prior written approval for any proposed transfer or issuance of ownership interests that results in the ownership (beneficial or of record) by any Person, or group of Persons acting in concert, of at least 10 percent of any class of your stock, partnership capital or membership interests.

§ 108.410 Changes in Control of NMVC Company (through change in ownership or otherwise).

You must obtain SBA's prior written approval for any proposed transaction or event that results in Control by any Person(s) not previously approved by SBA.

§ 108.420 Prohibition on exercise of ownership or Control rights in NMVC Company before SBA approval.

Without prior written SBA approval, no change of ownership or Control may take effect and no officer, director, employee or other Person acting on your behalf shall:

(a) Register on your books any transfer of ownership interest to the proposed new owner(s);

(b) Permit the proposed new owner(s) to exercise voting rights with respect to such ownership interest (including directly or indirectly procuring or voting any proxy, consent or authorization as to such voting rights at any meeting of shareholders, partners or members);

(c) Permit the proposed new owner(s) to participate in any manner in the conduct of your affairs (including exercising control over your books, records, funds or other assets; participating directly or indirectly in any disposition thereof; or serving as an officer, director, partner, manager, employee or agent); or

(d) Allow ownership or Control to pass to another Person.

§ 108.430 Notification to SBA of transactions that may change ownership or Control.

You must promptly notify SBA as soon as you have knowledge of transactions or events that may result in a transfer of Control or ownership of at least 10 percent of your capital. If there is any doubt as to whether a particular transaction or event will result in such a change, report the facts to SBA.

§ 108.440 Standards governing prior SBA approval for a proposed transfer of Control.

SBA approval is contingent upon full disclosure of the real parties in interest, the source of funds for the new owners' interest, and other data requested by SBA. As a condition of approving a proposed transfer of control, SBA may:

(a) Require an increase in your Regulatory Capital;

(b) Require the new owners or the transferee's Control Person(s) to assume, in writing, personal liability for your Leverage, effective only in the event of their direct or indirect participation in any transfer of Control not approved by SBA; or

(c) Require compliance with any other conditions set by SBA, including compliance with the requirements for minimum capital and management-ownership diversity as in effect at such time for new NMVC Companies.

§ 108.450 Notification to SBA of pledge of NMVC Company's shares.

(a) You must notify SBA in writing, within 30 calendar days, of the terms of any transaction in which:

(1) Any Person, or group of Persons acting in concert, pledges shares of your stock (or equivalent ownership interests) as collateral for indebtedness; and

(2) The shares pledged are at least 10 percent of your Regulatory Capital.

(b) If the transaction creates a change of ownership or Control, you must comply with § 108.400 or § 108.410, as appropriate.

Restrictions on Common Control or Ownership of Two or More NMVC Companies

§ 108.460 Restrictions on Common Control or ownership of two (or more) NMVC Companies.

Without SBA's prior written approval, you must not have an officer, director, manager, Control Person, or owner (with a direct or indirect ownership interest of at least 10 percent) who is also:

(a) An officer, director, manager, Control Person, or owner (with a direct or indirect ownership interest of at least 10 percent) of another NMVC Company; or

(b) An officer or director of any Person that directly or indirectly controls, or is controlled by, or is under Common Control with, another NMVC Company.

Change in Structure of NMVC Company

§ 108.470 SBA approval of merger, consolidation, or reorganization of NMVC Company.

You may not merge, consolidate, change form of organization (corporation or partnership) or reorganize without SBA's prior written approval. Any such merger or consolidation will be subject to § 108.440.

Subpart G—Managing the Operations of a NMVC Company

General Requirements

§ 108.500 Lawful operations under the Act.

You must engage only in the activities contemplated by the Act and in no other activities.

§ 108.502 Representations to the public.

You may not represent or imply to anyone that the SBA, the U.S. Government or any of its agencies or officers has approved any ownership interests you have issued or obligations you have incurred. Be certain to include a statement to this effect in any solicitation to investors. Example: You may not represent or imply that ''SBA stands behind the NMVC Company'' or that ''Your capital is safe because SBA's experts review proposed investments to make sure they are safe for the NMVC Company.''

§ 108.503 NMVC Company's adoption of an approved valuation policy.

(a) *Valuation guidelines.* You must prepare, document and report the valuations of your Loans and Investments in accordance with the Valuation Guidelines for SBICs issued by SBA. These guidelines may be obtained from SBA's Investment Division.

(b) *SBA approval of valuation policy.* You must have a written valuation policy approved by SBA for use in determining the value of your Loans and Investments. You must either:

(1) Adopt without change the model valuation policy set forth in section III of the Valuation Guidelines for SBICs; or

(2) Obtain SBA's prior written approval of an alternative valuation policy.

(c) *Responsibility for valuations.* Your board of directors, managing members, or general partner(s) will be solely responsible for adopting your valuation policy and for using it to prepare valuations of your Loans and Investments for submission to SBA. If SBA reasonably believes that your valuations, individually or in the aggregate, are materially misstated, it reserves the right to require you to engage, at your expense, an independent third party acceptable to SBA to substantiate the valuations.

(d) *Frequency of valuations.* (1) You must value your Loans and Investments at the end of the second quarter of your fiscal year, and at the end of your fiscal year.

(2) On a case-by-case basis, SBA may require you to perform valuations more frequently.

(3) You must report material adverse changes in valuations at least quarterly, within thirty days following the close of the quarter.

(e) *Review of valuations by independent public accountant.* (1) For valuations performed as of the end of your fiscal year, your independent public accountant must review your valuation procedures and the implementation of such procedures, including adequacy of documentation.

(2) The independent public accountant's report on your audited annual financial statements (SBA Form 468) must include a statement that your valuations were prepared in accordance with your approved valuation policy.

§ 108.504 Equipment and office requirements.

(a) *Computer capability.* You must have a personal computer with a modem, and be able to use this equipment to prepare reports (using SBA provided software) and transmit them to SBA. In addition, you must have access to the Internet and the capability to send and receive electronic mail via the Internet.

(b) *Facsimile capability.* You must be able to receive facsimile messages 24 hours per day at your primary office.

(c) *Accessible office.* You must maintain an office that is convenient to the public and is open for business during normal working hours.

§ 108.506 Safeguarding the NMVC Company's assets/Internal controls.

You must adopt a plan to safeguard your assets and monitor the reliability of your financial data, personnel, Portfolio, funds and equipment. You must provide your bank and custodian with a certified copy of your resolution or other formal document describing your control procedures.

§ 108.507 Violations based on false filings and nonperformance of agreements with SBA.

The following shall constitute a violation of this part:

(a) *Nonperformance.* Nonperformance of any of the requirements of any Debenture or of any written agreement with SBA.

(b) *False statement.* In any document submitted to SBA:

(1) Any false statement knowingly made; or

(2) Any misrepresentation of a material fact; or

(3) Any failure to state a material fact. A material fact is any fact that is necessary to make a statement not misleading in light of the circumstances under which the statement was made.

§ 108.509 Employment of SBA officials.

Without SBA's prior written approval, for a period of two years after the date of your most recent issuance of Leverage (or the receipt of any SBA Assistance as defined in part 105 of this chapter), you are not permitted to employ, offer employment to, or retain for professional services, any person who:

(a) Served as an officer, attorney, agent, or employee of SBA on or within one year before such date; and

(b) As such, occupied a position or engaged in activities which, in SBA's determination, involved discretion with respect to the granting of SBA Assistance.

Management and Compensation

§ 108.510 SBA approval of NMVC Company's Investment Adviser/Manager.

You may employ an Investment Adviser/Manager who will be subject to the supervision of your board of directors, managing members, or general partner. If you have Leverage or plan to seek Leverage, you must obtain SBA's prior written approval of the management contract. SBA's approval of an Investment Adviser/Manager for one NMVC Company does not indicate approval of that manager for any other NMVC Company.

(a) *Management contract.* The contract must:

(1) Specify the services the Investment Adviser/Manager will render to you and to the Small Businesses in your Portfolio, and

(2) Indicate the basis for computing Management Expenses.

(b) *Material change to approved management contract.* If there is a material change, both you and SBA must approve such change in advance. If you are uncertain if the change is material, submit the proposed revision to SBA.

§ 108.520 Management Expenses of a NMVC Company.

SBA must approve your initial Management Expenses and any increases in your Management Expenses.

(a) *Definition of Management Expenses.* Management Expenses include:

(1) Salaries;

(2) Office expenses;

(3) Travel;

(4) Business development;

(5) Office and equipment rental;

(6) Bookkeeping; and

(7) Expenses related to developing, investigating and monitoring investments.

(b) Management Expenses do not include services provided by specialized outside consultants, outside lawyers and independent public accountants, if they perform services not generally performed by a venture capital company.

Cash Management by a NMVC Company

§ 108.530 Restrictions on investments of idle funds by NMVC Companies.

(a) *Permitted investments of idle funds.* Funds not invested in Small Businesses must be maintained in:

(1) Direct obligations of, or obligations guaranteed as to principal and interest by, the United States, which mature within 15 months from the date of the investment, or

(2) Repurchase agreements with federally insured institutions, with a maturity of seven days or less. The securities underlying the repurchase agreements must be direct obligations of, or obligations guaranteed as to principal and interest by, the United States. The securities must be maintained in a custodial account at a federally insured institution; or

(3) Certificates of deposit with a maturity of one year or less, issued by a federally insured institution; or

(4) A deposit account in a federally insured institution, subject to a withdrawal restriction of one year or less; or

(5) A checking account in a federally insured institution; or

(6) A reasonable petty cash fund.

(b) *Deposit of funds in excess of the insured amount.* (1) You are permitted to deposit funds in a federally insured institution in excess of the institution's insured amount, but only if the institution is ''well capitalized'' in accordance with the definition set forth in regulations of the Federal Deposit Insurance Corporation, as amended (12 CFR 325.103).

(2) Exception: You may make a temporary deposit (not to exceed 30 days) in excess of the insured amount, in a transfer account established to facilitate the receipt and disbursement of funds or to hold funds necessary to honor Commitments issued.

(c) *Deposit of funds in Associate institution.* A deposit in, or a repurchase agreement with, a federally insured institution that is your Associate is not considered a Financing of such Associate under § 108.730, provided the terms of such deposit or repurchase agreement are no less favorable than those available to the general public.

Borrowing by NMVC Companies From NON-SBA Sources

§ 108.550 Prior approval of secured third-party debt of NMVC companies.

(a) *Definition.* In this § 108.550, ''secured third-party debt'' means any non-SBA debt secured by any of your assets, including secured guarantees and other contingent obligations that you voluntarily assume and secured lines of credit.

(b) *General rule.* You must get SBA's written approval before you incur any secured third-party debt or refinance any debt with secured third-party debt, including any renewal of a secured line of credit, increase in the maximum amount available under a secured line of credit, or expansion of the scope of a security interest or lien. For purposes of this paragraph (b), ''expansion of the scope of a security interest or lien'' does not include the substitution of one asset or group of assets for another, provided the asset values (as reported on your most recent annual Form 468) are comparable.

(c) *Conditions for SBA approval.* As a condition of granting its approval under this § 108.550, SBA may impose such restrictions or limitations as it deems appropriate, taking into account your historical performance, current financial position, proposed terms of the secured debt and amount of aggregate debt you will have outstanding (including Leverage). SBA will not favorably consider any requests for approval which include a blanket lien on all your assets, or a security interest in your investor commitments in excess of 125 percent of the proposed borrowing.

(d) *Thirty-day approval.* Unless SBA notifies you otherwise within 30 days after it receives your request, you may consider your request automatically approved if:

(1) You are in regulatory compliance;

(2) The security interest in your assets is limited to either those assets being acquired with the borrowed funds or an asset coverage ratio of no more than 2:1;

(3) Your request is for approval of a secured line of credit that would not cause your total outstanding borrowings (not including Leverage) to exceed 50 percent of your Leverageable Capital.

Voluntary Decrease in Regulatory Capital

§ 108.585 Voluntary decrease in NMVC Company's Regulatory Capital.

You must obtain SBA's prior written approval to reduce your Regulatory Capital by more than two percent in any fiscal year. At all times, you must retain sufficient Regulatory Capital to meet the minimum capital requirements in the Act and § 108.210, and sufficient Leverageable Capital to avoid having excess Leverage in violation of section 355(d) of the Act.

Subpart H—Recordkeeping, Reporting, and Examination Requirements for NMVC Companies

Recordkeeping Requirements for NMVC Companies

§ 108.600 General requirement for NMVC Company to maintain and preserve records.

(a) *Maintaining your accounting records.* You must establish and maintain your accounting records using SBA's standard chart of accounts for SBICs, unless SBA approves otherwise. You may obtain this chart of accounts from SBA.

(b) *Location of records.* You must keep the following records at your principal place of business or, in the case of paragraph (b)(3) of this section, at the branch office that is primarily responsible for the transaction:

(1) All your accounting and other financial records;

(2) All minutes of meetings of directors, stockholders, executive committees, partners, or other officials; and

(3) All documents and supporting materials related to your business transactions, except for any items held by a custodian under a written agreement between you and a Portfolio Concern or non-SBA lender, or any securities held in a safe deposit box, or by a licensed securities broker in an amount not exceeding the broker's per-account insurance coverage.

(c) *Preservation of records.* You must retain all the records that are the basis for your financial reports. Such records must be preserved for the periods specified in this paragraph (c), and must remain accessible for the first two years of the preservation period.

(1) You must preserve for at least 15 years or, in the case of a Partnership NMVC Company or LLC NMVC

Company, at least two years beyond the date of liquidation:

(i) All your accounting ledgers and journals, and any other records of assets, asset valuations, liabilities, equity, income, and expenses.

(ii) Your Articles, bylaws, minute books, and NMVC Company application.

(iii) All documents evidencing ownership of the NMVC Company including ownership ledgers, and ownership transfer registers.

(2) You must preserve for at least six years all supporting documentation (such as vouchers, bank statements, or canceled checks) for the records listed in paragraph (b)(l) of this section.

(3) After final disposition of any item in your Portfolio, you must preserve for at least six years:

(i) Financing applications and Financing instruments.

(ii) All loan, participation, and escrow agreements.

(iii) Size status declarations (SBA Form 480).

(iv) Any capital stock certificates and warrants of the Portfolio Concern that you did not surrender or exercise.

(v) All other documents and supporting material relating to the Portfolio Concern, including correspondence.

(4) You may substitute a microfilm or computer-scanned or generated copy for the original of any record covered by this paragraph (c).

(d) *Additional requirement.* You must comply with the recordkeeping and record retention requirements set forth in Circular A–110 of the Office of Management and Budget.

§ 108.610 Required certifications for Loans and Investments.

For each of your Loans and Investments, you must have the documents listed in this section. You must keep these documents in your files and make them available to SBA upon request.

(a) SBA Form 480, the Size Status Declaration, executed both by you and by the concern you are financing. By executing this document, both parties certify that the concern is a Small Business. For securities purchased from an underwriter in a public offering, you may substitute a prospectus showing that the concern is a Small Business.

(b) SBA Form 652, a certification by the concern you are financing that it will not illegally discriminate (see part 112 of this chapter).

(c) A certification by the concern you are financing of the intended use of the proceeds. For securities purchased from an underwriter in a public offering, you may substitute a prospectus indicating the intended use of proceeds.

(d) For each Low-Income Investment, a certification by the concern you are financing as to the basis for its qualification as a Low-Income Enterprise.

§ 108.620 Requirements to obtain information from Portfolio Concerns.

All the information required by this section is subject to the requirements of § 108.600 and must be in English.

(a) *Information for initial Financing decision.* Before extending any Financing, you must require the applicant to submit such financial statements, plans of operation (including intended use of financing proceeds), cash flow analyses, projections, and such community economic development information about the company, as are necessary to support your investment decision. The information submitted must be consistent with the size and type of the business and the amount of the proposed Financing.

(b) *Updated financial and community economic development information.* (1) The terms of each Financing must require the Portfolio Concern to provide, at least annually, sufficient financial and community economic development information to enable you to perform the following required procedures:

(i) Evaluate the financial condition of the Portfolio Concern for the purpose of valuing your investment;

(ii) Determine the continued eligibility of the Portfolio Concern;

(iii) Verify the use of Financing proceeds; and

(iv) Evaluate the community economic development impact of the Financing.

(2) The president, chief executive officer, treasurer, chief financial officer, general partner, or proprietor of the Portfolio Concern must certify the information submitted to you.

(3) For financial and valuation purposes, you may accept a complete copy of the Federal income tax return filed by the Portfolio Concern (or its proprietor) in lieu of financial statements, but only if appropriate for the size and type of the business involved.

(4) The requirements in this paragraph (b) do not apply when you acquire securities from an underwriter in a public offering (see § 108.825). In that case, you must keep copies of all reports furnished by the Portfolio Concern to the holders of its securities.

(c) *Information required for examination purposes.* You must obtain any information requested by SBA's examiners for the purpose of verifying the certifications made by a Portfolio Concern under § 108.610. In this regard, your Financing documents must contain provisions requiring the Portfolio Concern to give you and/or SBA's examiners access to its books and records for such purpose.

Reporting Requirements for NMVC Companies

§ 108.630 Requirement for NMVC companies to file financial statements and supplementary information with SBA (SBA Form 468).

(a) *Annual filing of Form 468.* For each fiscal year, you must submit to SBA financial statements and supplementary information prepared on SBA Form 468. You must file Form 468 on or before the last day of the third month following the end of your fiscal year, except for the information required under paragraphs (e) and (f) of this section, which must be filed on or before the last day of the fifth month following the end of your fiscal year.

(1) *Audit of Form 468.* An independent public accountant acceptable to SBA must audit the annual Form 468.

(2) *Insurance requirement for public accountant.* Unless SBA approves otherwise, your independent public accountant must carry at least $1,000,000 of Errors and Omissions insurance, or be self-insured and have a net worth of at least $1,000,000.

(b) *Interim filings of Form 468.* When requested by SBA, you must file interim reports on Form 468. SBA may require you to file the entire form or only certain statements and schedules. You must file such reports on or before the last day of the month following the end of the reporting period. When you submit a request for a draw under an SBA Leverage commitment, you must also comply with any applicable filing requirements set forth in § 108.1220.

(c) *Standards for preparation of Form 468.* You must prepare SBA Form 468 in accordance with SBA's Accounting Standards and Financial Reporting Requirements for Small Business Investment Companies, which you may obtain from SBA.

(d) *Where to file Form 468.* Submit all filings of Form 468 to the Office of New Markets Venture Capital in the Investment Division of SBA.

(e) *Reporting of social, economic, or community development impact information on Form 468.* Your annual filing of SBA Form 468 must include an assessment of the social, economic, or community development impact of each Financing. This assessment must specify the fulltime equivalent jobs

created, the impact of the Financing on the revenues and profits of the business and on taxes paid by the business and its employees, and a listing of the number and percentage of employees who reside in LI Areas.

(f) *Reporting of community development information.* For each Financing of a Low-Income Enterprise, your Form 468 must include an assessment of such Financing with respect to:

(1) The social, economic or community development benefits achieved as a result of the Financing;

(2) How and to what extent such benefits fulfilled the goals of your comprehensive business plan and Participation Agreement;

(3) Whether you consider the Financing or the results of the Financing to have fulfilled the objectives of the NMVC program; and

(4) Whether, and if so, how you achieved accountability to the residents of the LI Area in connection with that Financing.

§ 108.640 Requirement to file portfolio financing reports (SBA Form 1031).

For each Financing you make (excluding guarantees), you must submit a Portfolio Financing Report on SBA Form 1031 within 30 days of the closing date.

§ 108.650 Requirement to report portfolio valuations to SBA.

You must determine the value of your Loans and Investments in accordance with § 108.503. You must report such valuations to SBA within 90 days of the end of the fiscal year in the case of annual valuations, and within 30 days following the close of other reporting periods. You must report material adverse changes in valuations at least quarterly, within thirty days following the close of the quarter.

§ 108.660 Other items required to be filed by NMVC Company with SBA.

(a) *Reports to owners.* You must give SBA a copy of any report you furnish to your investors, including any prospectus, letter, or other publication concerning your financial operations or those of any Portfolio Concern.

(b) *Documents filed with SEC.* You must give SBA a copy of any report, application or document you file with the Securities and Exchange Commission.

(c) *Litigation reports.* When you become a party to litigation or other proceedings, you must give SBA a report within 30 days that describes the proceedings and identifies the other parties involved and your relationship to them.

(1) The proceedings covered by this paragraph (c) include any action by you, or by your security holder(s) in a personal or derivative capacity, against an officer, director, Investment Adviser or other Associate of yours for alleged breach of official duty.

(2) SBA may require you to submit copies of the pleadings and other documents SBA may specify.

(3) Where proceedings have been terminated by settlement or final judgment, you must promptly advise SBA of the terms.

(4) This paragraph (c) does not apply to collection actions or proceedings to enforce your ordinary creditors' rights.

(d) *Notification of criminal charges.* If any officer, director, or general partner of the NMVC Company, or any other person who was required by SBA to complete a personal history statement, is charged with or convicted of any criminal offense other than a misdemeanor involving a minor motor vehicle violation, you must report the incident to SBA within 5 calendar days. Such report must fully describe the facts that pertain to the incident.

(e) *Reports concerning Operational Assistance grant funds.* You must comply with all reporting requirements set forth in Circular A–110 of the Office of Management and Budget and any grant award document executed between you and SBA.

(f) *Other reports.* You must file any other reports SBA may require in writing.

§ 108.680 Reporting changes in NMVC Company not subject to prior SBA approval.

(a) *Changes to be reported for post-approval.* This section applies to any changes in your Articles, ownership, capitalization, management, operating area, or investment policies that do not require SBA's prior approval. You must report such changes to SBA within 30 days for post approval.

(b) *Approval by SBA.* You may consider any change submitted under this § 108.680 to be approved unless SBA notifies you to the contrary within 90 days after receiving it. SBA's approval is contingent upon your full disclosure of all relevant facts and is subject to any conditions SBA may prescribe.

Examinations of NMVC Companies by SBA for Regulatory Compliance

§ 108.690 Examinations.

All NMVC companies must submit to annual examinations by or at the direction of SBA for the purpose of evaluating regulatory compliance.

§ 108.691 Responsibilities of NMVC Company during examination.

You must make all books, records and other pertinent documents and materials available for the examination, including any information required by the examiner under § 108.620(c). In addition, the agreement between you and the independent public accountant performing your audit must provide that any information in the accountant's working papers be made available to SBA upon request.

§ 108.692 Examination fees.

(a) *General.* SBA will assess fees for examinations in accordance with this § 108.692. Unless SBA determines otherwise on a case by case basis, SBA will not assess fees for special examinations to obtain specific information.

(b) *Base fee.* A base fee of $3,500 will be assessed, subject to adjustment in accordance with paragraph (c) of this section.

(c) *Adjustments to base fee.* The base fee will be decreased based on the following criteria:

(1) If you have no outstanding regulatory violations at the time of the commencement of the examination and SBA did not identify any violations as a result of the most recent prior examination, you will receive a 15% discount on your base fee; and

(2) If you were fully responsive to the letter of notification of examination (that is, you provided all requested documents and information within the time period stipulated in the notification letter in a complete and accurate manner, and you prepared and had available all information requested by the examiner for on-site review), you will receive a 10% discount on your base fee.

(d) *Delay fee.* If, in the judgment of SBA, the time required to complete your examination is delayed due to your lack of cooperation or the condition of your records, SBA may assess an additional fee of up to $500 per day.

Subpart I—Financing of Small Businesses by NMVC Companies

Determining the Eligibility of a Small Business for NMVC Financing

§ 108.700 Compliance with size standards in part 121 of this chapter as a condition of Assistance.

You are permitted to provide financial assistance and management services only to a Small Business. To determine whether an applicant meets the size standards for a Small Business, you may use either the financial size standards in § 121.301(c)(1) of this chapter or the

industry standard covering the industry in which the applicant is primarily engaged, as set forth in § 121.301(c)(2) of this chapter.

§ 108.710 Requirement to finance Low-Income Enterprises.

(a) *Low-Income Enterprise Financings.* At the close of each of your fiscal years:

(1) At least 80 percent of your Portfolio Concerns must be Low-Income Enterprises in which you have an Equity Capital Investment; and

(2) For all Financings you have extended, you must have invested at least 80 percent (in total dollars) in Equity Capital Investments in Low-Income Enterprises.

(b) *Non-compliance with this section.* If you have not reached the percentages required in paragraph (a) of this section at the end of any fiscal year, then you must be in compliance by the end of the following fiscal year. However, you will not be eligible for additional Leverage until such time as you reach the required percentages (see § 108.1120).

§ 108.720 Small Businesses that may be ineligible for financing.

(a) *Relenders or reinvestors.* You are not permitted to finance any business that is a relender or reinvestor. Relenders or reinvestors are businesses whose primary business activity involves, directly or indirectly, providing funds to others, purchasing debt obligations, factoring, or long-term leasing of equipment with no provision for maintenance or repair.

(b) *Passive Businesses.* You are not permitted to finance a passive business.

(1) *Definition.* A business is passive if:

(i) It is not engaged in a regular and continuous business operation (for purposes of this paragraph (b), the mere receipt of payments such as dividends, rents, lease payments, or royalties is not considered a regular and continuous business operation); or

(ii) Its employees are not carrying on the majority of day to day operations, and the company does not provide effective control and supervision, on a day to day basis, over persons employed under contract; or

(iii) It passes through substantially all of the proceeds of the Financing to another entity.

(2) *Exception for pass-through of proceeds to subsidiary.* With the prior written approval of SBA, you may finance a passive business if it is a Small Business and it passes substantially all the proceeds through to one or more subsidiary companies, each of which is an eligible Small Business that is not passive. For the purpose of this paragraph (b) (2), ''subsidiary company'' means a company in which at least 50 percent of the outstanding voting securities are owned by the Financed passive business.

(3) *Exception for certain Partnership NMVC companies.* With the prior written approval of SBA, if you are a Partnership NMVC Company, you may form one or more wholly owned corporations in accordance with this paragraph (b) (3). The sole purpose of such corporation(s) must be to provide Financing to one or more eligible, unincorporated Small Businesses. You may form such corporation(s) only if a direct Financing to such Small Businesses would cause any of your investors to incur unrelated business taxable income under section 511 of the Internal Revenue Code of 1986, as amended (26 U.S.C. 511). Your investment of funds in such corporation(s) will not constitute a violation of § 108.730(a).

(c) *Real Estate Businesses.* (1)You are not permitted to finance:

(i) Any business classified under sector 233 (Building, Developing, and Contracting) of the NAICS Manual, or

(ii) Any business listed under sector 531 (Real Estate) unless at least 80 percent of the revenue is derived from non-Affiliate sources.

(2) You are not permitted to finance a business, regardless of NAICS classification, if the Financing is to be used to acquire or refinance real property, unless the Small Business:

(i) Is acquiring an existing property and will use at least 51 percent of the usable square footage for an eligible business purpose; or

(ii) Is building or renovating a building and will use at least 67 percent of the usable square footage for an eligible business purpose; or

(iii) Occupies the subject property and uses at least 67 percent of the usable square footage for an eligible business purpose.

(d) *Project Financing.* You are not permitted to finance a business if:

(1) The assets of the business are to be reduced or consumed, generally without replacement, as the life of the business progresses, and the nature of the business requires that a stream of cash payments be made to the business's financing sources, on a basis associated with the continuing sale of assets. Examples include real estate development projects and oil and gas wells; or

(2) The primary purpose of the Financing is to fund production of a single item or defined limited number of items, generally over a defined production period, and such production will constitute the majority of the activities of the Small Business. Examples include motion pictures and electric generating plants.

(e) *Farm land purchases.* You are not permitted to finance the acquisition of farmland. Farmland means land, which is or is intended to be used for agricultural or forestry purposes, such as the production of food, fiber, or wood, or is so taxed or zoned.

(f) *Public interest.* You are not permitted to finance any business if the proceeds are to be used for purposes contrary to the public interest, including but not limited to activities which are in violation of law, or inconsistent with free competitive enterprise.

(g) *Foreign investment.* (1) General rule. You are not permitted to finance a business if:

(i) The funds will be used substantially for a foreign operation; or

(ii) At the time of the Financing or within one year thereafter, more than 49 percent of the employees or tangible assets of the Small Business are located outside the United States (unless you can show, to SBA's satisfaction, that the Financing was used for a specific domestic purpose).

(2) *Exception.* This paragraph (g) does not prohibit a Financing used to acquire foreign materials and equipment or foreign property rights for use or sale in the United States.

(h) *Financing NMVC companies or SBICs.* You are not permitted to provide funds, directly or indirectly, that the Small Business will use:

(1) To purchase stock in or provide capital to a NMVC Company or SBIC; or

(2) To repay an indebtedness incurred for the purpose of investing in a NMVC Company or SBIC.

§ 108.730 Financings which constitute conflicts of interest.

(a) *General rule.* You must not self-deal to the prejudice of a Small Business, the NMVC Company, its shareholders or partners, or SBA. Unless you obtain a prior written exemption from SBA for special instances in which a Financing may further the purposes of the Act despite presenting a conflict of interest, you must not directly or indirectly:

(1) Provide Financing to any of your Associates, except for a Small Business that satisfies all of the following conditions:

(i) Your Associate relationship with the Small Business is described by paragraph (8) or (9) of the definition of Associate in § 108.50,

(ii) No Person triggering the Associate relationship identified in paragraph (a)(1)(i) of this section is a Close Relative or Secondary Relative of any

Person described in paragraphs (1), (2), (4), or (5) of the definition of Associate in § 108.50, and

(iii) No single Associate of yours has either a voting interest or an economic interest in the Small Business exceeding 20 percent, and no two or more of your Associates have either a voting interest or an economic interest exceeding 33 percent. Economic interests shall be computed on a fully diluted basis, and both voting and economic interests shall exclude any interest owned through the NMVC Company.

(2) Provide Financing to an Associate of another NMVC Company if one of your Associates has received or will receive any direct or indirect Financing or a Commitment from that NMVC Company or a third NMVC Company (including Financing or Commitments received under any understanding, agreement, or cross dealing, reciprocal or circular arrangement).

(3) Borrow money from:

(i) A Small Business Financed by you;

(ii) An officer, director, or owner of at least a 10 percent equity interest in such business; or

(iii) A Close Relative of any such officer, director, or equity owner.

(4) Provide Financing to a Small Business to discharge an obligation to your Associate or free other funds to pay such obligation. This paragraph (a)(4) does not apply if the obligation is to an Associate Lending Institution and is a line of credit or other obligation incurred in the normal course of business.

(b) *Rules applicable to Associates.* Without SBA' s prior written approval, your Associates must not, directly or indirectly:

(1) Borrow money from any Person described in paragraph (a)(3) of this section.

(2) Receive from a Small Business any compensation in connection with Assistance you provide (except as permitted under § 108.825(c)), or anything of value for procuring, attempting to procure, or influencing your action with respect to such Assistance.

(c) *Applicability of other laws.* You are also bound by any restrictions in Federal or State laws governing conflicts of interest and fiduciary obligations.

(d) *Financings with Associates*— (1) *Financings with Associates requiring prior approval.* Without SBA's prior written approval, you may not Finance any business in which your Associate has either a voting equity interest or total equity interests (including potential interests) of at least five percent, except as otherwise permitted under paragraph (a)(1) of this section.

(2) *Other Financings with Associates.* If you and an Associate provide Financing to the same Small Business, either at the same time or at different times, you must be able to demonstrate to SBA's satisfaction that the terms and conditions are (or were) fair and equitable to you, taking into account any differences in the timing of each party's financing transactions.

(3) *Exceptions to paragraphs (d)(l) and (d)(2) of this section.* A Financing that falls into one of the following categories is exempt from the prior approval requirement in paragraph (d)(1) of this section or is presumed to be fair and equitable to you for the purposes of paragraph (d)(2) of this section, as appropriate:

(i) Your Associate is a Lending Institution that is providing financing under a credit facility in order to meet the operational needs of the Small Business, and the terms of such financing are usual and customary.

(ii) Your Associate invests in the Small Business on the same terms and conditions and at the same time as you.

(iii) Both you and your Associate are NMVC companies.

(e) *Use of Associates to manage Portfolio Concerns.* To protect your investment, you may designate an Associate to serve as an officer, director, or other participant in the management of a Small Business. You must identify any such Associate in your records available for SBA's review under § 108.600. Without SBA's prior written approval, the Associate must not:

(1) Have any other direct or indirect financial interest in the Portfolio Concern that exceeds, or has the potential to exceed, the percentages of the Portfolio Concern's equity set forth in paragraph (a)(1) of this section.

(2) Receive any income or anything of value from the Portfolio Concern unless it is for your benefit, with the exception of director's fees, expenses, and distributions based upon the Associate's ownership interest in the Concern.

(f) *1940 and 1980 Act Companies: SEC exemptions.* If you are a 1940 or 1980 Act Company and you receive an exemption from the Securities and Exchange Commission for a transaction described in this § 108.730, you need not obtain SBA's approval of the transaction. However, you must promptly notify SBA of the transaction.

(g) *Restriction on options obtained by NMVC Company's management and employees.* Your employees, officers, directors, managing members or general partners, or the general partners of the management company that is providing services to you or to your general partner, may obtain options in a Financed Small Business only if:

(1) They participate in the Financing on a *pari passu* basis with you; or

(2) SBA gives its prior written approval; or

(3) The options received are compensation for service as a member of the board of directors of the Small Business, and such compensation does not exceed that paid to other outside directors. In the absence of such directors, fees must be reasonable when compared with amounts paid to outside directors of similar companies.

§ 108.740 Portfolio diversification (''overline'' limitation).

(a) Without SBA's prior written approval, you may provide Financing or a Commitment to a Small Business only if the resulting amount of your aggregate outstanding Financings and Commitments to such Small Business and its Affiliates does not exceed 20 percent of the sum of:

(1) Your Regulatory Capital as of the date of the Financing or Commitment; plus

(2) Any permitted Distribution(s) you made during the five years preceding the date of the Financing or Commitment which reduced your Regulatory Capital.

(b) For the purposes of paragraph (a) of this section, you must measure each outstanding Financing at its current cost plus any amount of the Financing that was previously written off.

§ 108.760 How a change in size or activity of a Portfolio Concern affects the NMVC Company and the Portfolio Concern.

(a) *Effect on NMVC Company of a change in size of a Portfolio Concern.* If a Portfolio Concern no longer qualifies as a Small Business you may keep your investment in the concern and:

(1) Subject to the overline limitations of § 108.740, you may provide additional Financing to the concern up to the time it makes a public offering of its securities.

(2) Even after the concern makes a public offering, you may exercise any stock options, warrants, or other rights to purchase Equity Securities which you acquired before the public offering, or fund Commitments you made before the public offering.

(b) *Effect of a change in business activity occurring within one year of NMVC Company's initial Financing*— (1) *Retention of Investment.* Unless you receive SBA's written approval, you may not keep your investment in a Portfolio Concern, small or otherwise, which becomes ineligible by reason of a change in its business activity within one year of your initial investment.

(2) *Request for SBA 's approval to retain investment.* If you request that SBA approve the retention of your investment, your request must include sufficient evidence to demonstrate that the change in business activity was caused by an unforeseen change in circumstances and was not contemplated at the time the Financing was made.

(3) *Additional Financing.* If SBA approves your request to retain an investment under paragraph (b)(2) of this section, you may provide additional Financing to the Portfolio Concern to the extent necessary to protect against the loss of the amount of your original investment, subject to the overline limitations of § 108.740.

(c) *Effect of a change in business activity occurring more than one year after the initial Financing.* If a Portfolio Concern becomes ineligible because of a change in business activity more than one year after your initial Financing you may:

(1) Retain your investment: and

(2) Provide additional Financing to the Portfolio Concern to the extent necessary to protect against the loss of the amount of your original investment, subject to the overline limitations of § 108.740.

Structuring NMVC Company's Financing of Eligible Small Businesses

§ 108.800 Financings in the form of equity interests.

You may not, inadvertently or otherwise:

(a) Become a general partner in any unincorporated business; or

(b) Become jointly or severally liable for any obligations of an unincorporated business.

§ 108.820 Financings in the form of guarantees.

(a) *General rule.* At the request of a Small Business or where necessary to protect your existing investment, you may guarantee the monetary obligation of a Small Business to any non-Associate creditor.

(b) *Exception.* You may not issue a guaranty if:

(1) You would become subject to State regulation as an insurance, guaranty or surety business; or

(2) The amount of the guaranty plus any direct Financings to the Small Business exceed the overline limitations of § 108.740, except that a pledge of the Equity Securities of the issuer or a subordination of your lien or creditor position does not count toward your overline.

(c) *Pledge of NMVC Company's assets as guaranty.* For purposes of this section, a guaranty with recourse only to specific asset(s) you have pledged is equal to the fair market value of such asset(s) or the amount of the debt guaranteed, whichever is less.

§ 108.825 Purchasing securities from an underwriter or other third party.

(a) *Securities purchased through or from an underwriter.* You may purchase the securities of a Small Business through or from an underwriter if:

(1) You purchase such securities within 90 days of the date the public offering is first made;

(2) Your purchase price is no more than the original public offering price; and

(3) The amount paid by you for the securities (less ordinary and reasonable underwriting charges and commissions) has been, or will be, paid to the Small Business, and the underwriter certifies in writing that this requirement has been met.

(b) *Recordkeeping requirements.* You must keep records available for SBA's inspection which show the relevant details of the transaction, including, but not limited to, date, price, commissions, and the underwriter's certifications required under paragraphs (a)(3) and (c) of this section.

(c) *Underwriter's requirements.* The underwriter must certify whether it is your Associate. You may pay reasonable and customary commissions and expenses to an Associate underwriter for the portion of an offering that you purchase.

(d) *Securities purchased from another NMVC Company or from SBA.* You may purchase from, or exchange with, another NMVC Company, Portfolio securities (or any interest therein). Such purchase or exchange may only be made on a non-recourse basis. You may not have more than one-third of your total assets (valued at cost) invested in such securities. If you have previously sold Portfolio securities (or any interest therein) on a recourse basis, you shall include the amount for which you may be contingently liable in your overline computation.

(e) *Purchases of securities from other non-issuers.* You may purchase securities of a Small Business from a non-issuer not previously described in this § 108.825 if such acquisition is a reasonably necessary part of the overall sound Financing of the Small Business.

Limitations on Disposition of Assets

§ 108.885 Disposition of assets to NMVC Company's Associates.

Except with SBA's prior written approval, you are not permitted to dispose of assets (including assets acquired in liquidation) to any Associate. As a prerequisite to such approval, you must demonstrate that the proposed terms of disposal are at least as favorable to you as the terms obtainable elsewhere.

Subpart J—SBA Financial Assistance for NMVC Companies (Leverage)

General Information About Obtaining Leverage

§ 108.1100 Type of Leverage and application procedures.

(a) *Type of Leverage available.* You may apply for Leverage from SBA in the form of a guarantee of your Debentures.

(b) *Applying for Leverage.* The Leverage application process has two parts. You must first apply for SBA's conditional commitment to reserve a specific amount of Leverage for your future use. You may then apply to draw down Leverage against the commitment. See §§ 108.1200 through 108.1240.

(c) *Where to send your application.* Send all Leverage applications to SBA, Investment Division Office of New Markets Venture Capital, 409 Third Street, S.W., Washington, DC 20416.

§ 108.1120 General eligibility requirement for Leverage.

To be eligible for Leverage, you must be in compliance with the Act, the regulations in this part, and your Participation Agreement.

§ 108.1130 Leverage fees payable by NMVC Company.

There is no fee for the issuance of Debentures by a NMVC Company.

§ 108.1140 NMVC Company's acceptance of SBA remedies under § 108.1810.

If you issue Leverage, you automatically agree to the terms and conditions in § 108.1810 as it exists at the time of issuance. The effect of these terms and conditions is the same as if they were fully incorporated in the terms of your Leverage.

Maximum Amount of Leverage for Which a NMVC Company Is Eligible

§ 108.1150 Maximum amount of Leverage for a NMVC Company.

The face amount of a NMVC Company's outstanding Debentures may not exceed 150 percent of its Leverageable Capital.

Conditional Commitments by SBA To Reserve Leverage for a NMVC Company

§ 108.1200 SBA's Leverage commitment to a NMVC Company—application procedure, amount, and term.

(a) *General.* Under the provisions in §§ 108.1200 through 108.1240, you may

apply for SBA's conditional commitment to reserve a specific amount and type of Leverage for your future use. You may then apply to draw down Leverage against the commitment.

(b) *Applying for a Leverage commitment.* SBA will notify you when it is accepting requests for Leverage commitments. Upon receipt of your request, SBA will send you a complete application package.

(c) *Limitations on the amount of a Leverage commitment.* The amount of a Leverage commitment must be a multiple of $5,000. SBA, in its discretion, may determine a minimum dollar amount for Leverage commitments. Any such minimum amounts will be published in Notices in the **Federal Register** from time to time.

(d) *Term of Leverage commitment.* SBA's Leverage commitment will automatically lapse on the expiration date stated in the commitment letter issued to you by SBA.

§ 108.1220 Requirement for NMVC Company to file financial statements at the time of request for a draw.

(a) If you submit a request for a draw against SBA's Leverage commitment more than 90 days since your submission of an annual Form 468 or a Form 468 (Short Form), you must:

(1) Give SBA a financial statement on Form 468 (Short Form), and

(2) File a statement of no material adverse change in your financial condition since your last filing of Form 468.

(b) You will not be eligible for a draw if you are not in compliance with this § 108.1220.

§ 108.1230 Draw-downs by NMVC Company under SBA's Leverage commitment.

(a) *NMVC Company's authorization of SBA to guarantee securities.* By submitting a request for a draw against SBA's Leverage commitment, you authorize SBA, or any agent or trustee SBA designates, to guarantee your Debenture and to sell it with SBA's guarantee.

(b) *Limitations on amount of draw.* The amount of a draw must be a multiple of $5,000. SBA, in its discretion, may determine a minimum dollar amount for draws against SBA's Leverage commitments. Any such minimum amounts will be published in Notices in the **Federal Register** from time to time.

(c) *Effect of regulatory violations on NMVC Company's eligibility for draws*—(1) *General rule.* You are eligible to make a draw against SBA's Leverage commitment only if you are in compliance with all applicable provisions of the Act and SBA regulations (i.e., no unresolved statutory or regulatory violations) and your Participation Agreement.

(2) *Exception to general rule.* If you are not in compliance, you may still be eligible for draws if:

(i) SBA determines that your outstanding violations are of non-substantive provisions of the Act or regulations or your Participation Agreement and that you have not repeatedly violated any non-substantive provisions; or

(ii) You have agreed with SBA on a course of action to resolve your violations and such agreement does not prevent you from issuing Leverage.

(d) *Procedures for funding draws.* You may request a draw at any time during the term of the commitment. With each request, submit the following documentation:

(1) A statement certifying that there has been no material adverse change in your financial condition since your last filing of SBA Form 468 (see also § 108.1220 for SBA Form 468 filing requirements).

(2) If your request is submitted more than 30 days following the end of your fiscal year, but before you have submitted your annual filing of SBA Form 468 (Long Form) in accordance with § 108.630(a), a preliminary unaudited annual financial statement on SBA Form 468 (Short Form).

(3) A statement certifying that to the best of your knowledge and belief, you are in compliance with all provisions of the Act and SBA regulations (i.e., no unresolved regulatory or statutory violations) and your Participation Agreement, or a statement listing any specific violations you are aware of. Either statement must be executed by one of the following:

(i) An officer of the NMVC Company;

(ii) An officer of a corporate general partner of the NMVC Company;

(iii) An individual who is authorized to act as or for a general partner of the NMVC Company; or

(iv) An individual who is authorized to act as or for a member-manager of the NMVC Company.

(4) A statement that the proceeds are needed to fund one or more particular Small Businesses or to provide liquidity for your operations. If required by SBA, the statement must include the name and address of each Small Business, and the amount and anticipated closing date of each proposed Financing.

(e) *Reporting requirements after drawing funds.* (1) Within 30 calendar days after the actual closing date of each Financing funded with the proceeds of your draw, you must file an SBA Form 1031 confirming the closing of the transaction.

(2) If SBA required you to provide information concerning a specific planned Financing under paragraph (d)(4) of this section, and such Financing has not closed within 60 calendar days after the anticipated closing date, you must give SBA a written explanation of the failure to close.

(3) If you do not comply with this paragraph (e), you will not be eligible for additional draws. SBA may also determine that you are not in compliance with the terms of your Leverage under § 108.1810.

§ 108.1240 Funding of NMVC Company's draw request through sale to third-party.

(a) *NMVC Company's authorization of SBA to arrange sale of securities to third-party.* By submitting a request for a draw of Debenture Leverage, you authorize SBA, or any agent or trustee SBA designates, to enter into any agreements (and to bind you to such agreements) necessary to accomplish:

(1) The sale of your Debenture to a third-party at a rate approved by SBA; and

(2) The purchase of your security from the third-party and the pooling of your security with other securities with the same maturity date.

(b) *Sale of Debentures to a third-party.* If SBA arranges for the sale of your Debenture to a third-party, the sale price may be an amount discounted from the face amount of the Debenture.

Funding Leverage by Use of SBA Guaranteed Trust Certificates ("TCs")

§ 108.1600 SBA authority to issue and guarantee Trust Certificates.

(a) *Authorization.* Section 356 of the Act authorizes SBA to issue TCs and to guarantee the timely payment of the principal and interest thereon. Any guarantee by SBA of such TC is limited to the principal and interest due on the Debentures in any Trust or Pool backing such TC. The full faith and credit of the United States is pledged to the payment of all amounts due under the guarantee of any TC.

(b) *SBA authority to arrange public or private fundings of Leverage.* SBA in its discretion may arrange for public or private financing under its guarantee authority. Such financing arranged by SBA may be accomplished by the sale of individual Debentures, aggregations of Debentures, or Pools or Trusts of Debentures.

(c) *Pass-through provisions.* TCs shall provide for a pass-through to their holders of all amounts of principal and

interest paid on the Debentures in the Pool or Trust against which they are issued.

(d) *Formation of a Pool or Trust holding Leverage Securities.* SBA shall approve the formation of each Pool or Trust. SBA may, in its discretion, establish the size of the Pools and their composition, the interest rate on the TCs issued against Trusts or Pools, fees, discounts, premiums and other charges made in connection with the Pools, Trusts, and TCs, and any other characteristics of a Pool or Trust it deems appropriate.

§ 108.1610 Effect of prepayment or early redemption of Leverage on a Trust Certificate.

(a) The rights, if any, of a NMVC Company to prepay any Debenture is established by the terms of such security, and no such right is created or denied by the regulations in this part.

(b) SBA's rights to purchase or prepay any Debenture without premium are established by the terms of the Guaranty Agreement relating to the Debenture.

(c) Any prepayment of a Debenture pursuant to the terms of the Guaranty Agreement relating to such security shall reduce the SBA guarantee of timely payment of principal and interest on a TC in proportion to the amount of principal that such prepaid Debenture represents in the Trust or Pool backing such TC.

(d) SBA shall be discharged from its guarantee obligation to the holder or holders of any TC, or any successor or transferee of such holder, to the extent of any such prepayment. whether or not such successor or transferee shall have notice of any such prepayment.

(e) Interest on prepaid Debentures shall accrue only through the date of prepayment.

(f) In the event that all Debentures constituting a Trust or Pool are prepaid, the TCs backed by such Trust or Pool shall be redeemed by payment of the unpaid principal and interest on the TCs; provided, however, that in the case of the prepayment of a Debenture pursuant to the provisions of the Guaranty Agreement relating to the Debenture, the CRA shall pass through pro rata to the holders of the TCs any such prepayments including any prepayment penalty paid by the obligor NMVC Company pursuant to the terms of the Debenture.

§ 108.1620 Functions of agents, including Central Registration Agent, Selling Agent and Fiscal Agent.

(a) *Agents.* SBA may appoint or cause to be appointed agent(s) to perform functions necessary to market and service Debentures or TCs pursuant to this part.

(1) *Selling Agent.* As a condition of guaranteeing a Debenture, SBA may cause each NMVC Company to appoint a Selling Agent to perform functions that include, but are not limited to:

(i) Selecting qualified entities to become pool or Trust assemblers (''Poolers'').

(ii) Receiving guaranteed Debentures as well as negotiating the terms and conditions of sales or periodic offerings of Debentures and/or TCs on behalf of NMVC companies.

(iii) Directing and coordinating periodic sales of Debentures and/or TCs.

(iv) Arranging for the production of Offering Circulars, certificates, and such other documents as may be required from time to time.

(2) *Fiscal Agent.* SBA shall appoint a Fiscal Agent to:

(i) Establish performance criteria for Poolers.

(ii) Monitor and evaluate the financial markets to determine those factors that will minimize or reduce the cost of funding Debentures.

(iii) Monitor the performance of the Selling Agent, Poolers, CRA, and the Trustee.

(iv) Perform such other functions as SBA, from time to time, may prescribe.

(3) *Central Registration Agent.* Pursuant to a contract entered into with SBA, the CRA, as SBA's agent, will do the following with respect to the Pools or Trust Certificates for the Debentures:

(i) Form an SBA-approved Pool or Trust;

(ii) Issue the TCs in the form prescribed by SBA;

(iii) Transfer the TCs upon the sale of original issue TCs in any secondary market transaction;

(iv) Receive payments from NMVC companies;

(v) Make periodic payments as scheduled or required by the terms of the TCs, and pay all amounts required to be paid upon prepayment of Debentures;

(vi) Hold, safeguard, and release all Debentures constituting Trusts or Pools upon instructions from SBA;

(vii) Remain custodian of such other documentation as SBA shall direct by written instructions;

(viii) Provide for the registration of all pooled Debentures, all Pools and Trusts, and all TCs;

(ix) Perform such other functions as SBA may deem necessary to implement the provisions of this section.

(b) *Functions.* Either SBA or an agent appointed by SBA may perform the function of locating purchasers, and negotiating and closing the sale of Debentures and TCs. Nothing in the regulations in this part shall be interpreted to prevent the CRA from acting as SBA's agent for this purpose.

§ 108.1630 SBA regulation of Brokers and Dealers and disclosure to purchasers of Leverage or Trust Certificates.

(a) *Brokers and Dealers.* Each broker, dealer, and Pool or Trust assembler approved by SBA pursuant to these regulations shall either be regulated by a Federal financial regulatory agency, or be a member of the National Association of Securities Dealers (NASD), and shall be in good standing in respect to compliance with the financial, ethical, and reporting requirements of such body. They also shall be in good standing with SBA as determined by the SBA Associate Administrator for Investment (see paragraph (c) of this section) and shall provide a fidelity bond or insurance in such amount as SBA may require.

(b) *Suspension and/or termination of Broker or Dealer.* SBA shall exclude from the sale and all other dealings in Debentures or TCs any broker or dealer:

(1) If such broker's or dealer's authority to engage in the securities business has been revoked or suspended by a supervisory agency. When such authority has been suspended, SBA will suspend such broker or dealer for the duration of such suspension by the supervisory agency.

(2) If such broker or dealer has been indicted or otherwise formally charged with a misdemeanor or felony bearing on its fitness, such broker or dealer may be suspended while the charge is pending. Upon conviction, participation may be terminated.

(3) If such broker or dealer has suffered an adverse final civil judgment holding that such broker or dealer has committed a breach of trust or violation of law or regulation protecting the integrity of business transactions or relationships, participation in the market for Debentures or TCs may be terminated.

(c) *Termination/suspension proceedings.* A broker's or dealer's participation in the market for Debentures or TCs will be conducted in accordance with part 134 of this chapter. SBA may, for any of the reasons stated in paragraphs (b) (1) through (b)(3) of this section, suspend the privilege of any broker or dealer to participate in this market. SBA shall give written notice at least ten (10) business days prior to the effective date of such suspension. Such notice shall inform the broker or dealer of the opportunity for a hearing pursuant to part 134 of this chapter.

§ 108.1640 SBA access to records of the CRA, Brokers, Dealers and Pool or Trust assemblers.

The CRA and any broker, dealer and Pool or Trust assembler operating under the regulations in this part shall make all books, records and related materials associated with Debentures and TCs available to SBA for review and copying purposes. Such access shall be at such party's primary place of business during normal business hours.

Miscellaneous

§ 108.1700 Transfer by SBA of its interest in a NMVC Company's Leverage security.

Upon such conditions and for such consideration as it deems reasonable, SBA may sell, assign, transfer, or otherwise dispose of any Debenture held by or on behalf of SBA. Upon notice by SBA, a NMVC Company will make all payments of principal and interest as shall be directed by SBA. A NMVC Company will be liable for all damage or loss which SBA may sustain by reason of such disposal, up to the amount of the NMVC Company's liability under such security, plus court costs and reasonable attorney's fees incurred by SBA.

§ 108.1710 SBA authority to collect or compromise its claims.

SBA may, upon such conditions and for such consideration as it deems reasonable, collect or compromise all claims relating to obligations held or guaranteed by SBA, and all legal or equitable rights accruing to SBA.

§ 108.1720 Characteristics of SBA's guarantee.

If SBA agrees to guarantee a NMVC Company's Debentures, such guarantee will be unconditional, irrespective of the validity, regularity or enforceability of the Debentures or any other circumstances that might constitute a legal or equitable discharge or defense of a guarantor. Pursuant to its guarantee, SBA will make timely payments of principal and interest on the Debentures.

Subpart K—NMVC Company's Noncompliance With Terms of Leverage

§ 108.1810 Events of default and SBA's remedies for NMVC Company's noncompliance with terms of Debentures.

(a) *Applicability of this section.* By issuing Debentures, you automatically agree to the terms, conditions and remedies in this section, as in effect at the time of issuance and as if fully set forth in the Debentures.

(b) *Automatic events of default.* The occurrence of one or more of the events in this paragraph (b) causes the remedies in paragraph (c) of this section to take effect immediately.

(1) *Insolvency.* You become equitably or legally insolvent.

(2) *Voluntary assignment.* You make a voluntary assignment for the benefit of creditors without SBA's prior written approval.

(3) *Bankruptcy.* You file a petition to begin any bankruptcy or reorganization proceeding, receivership, dissolution or other similar creditors' rights proceeding, or such action is initiated against you and is not dismissed within 60 days.

(c) *SBA remedies for automatic events of default.* Upon the occurrence of one or more of the events in paragraph (b) of this section:

(1) Without notice, presentation or demand, the entire indebtedness evidenced by your Debentures, including accrued interest, and any other amounts owed SBA with respect to your Debentures, is immediately due and payable; and

(2) You automatically consent to the appointment of SBA or its designee as your receiver under section 363(c) of the Act.

(d) *Events of default with notice.* For any occurrence (as determined by SBA) of one or more of the events in this paragraph (d), SBA may avail itself of one or more of the remedies in paragraph (e) of this section.

(1) *Fraud.* You commit a fraudulent act that causes detriment to SBA's position as a creditor or guarantor.

(2) *Fraudulent transfers.* You make any transfer or incur any obligation that is fraudulent under the terms of 11 U.S.C. 548.

(3) *Willful conflicts of interest.* You willfully violate § 108.730.

(4) *Willful non-compliance.* You willfully violate one or more of the substantive provisions of the Act or any substantive regulation promulgated under the Act or any substantive provision of your Participation Agreement.

(5) *Repeated Events of Default.* At any time after being notified by SBA of the occurrence of an event of default under paragraph (f) of this section, you engage in similar behavior that results in another occurrence of the same event of default.

(6) *Transfer of Control.* You willfully violate § 108.410, and as a result of such violation you undergo a transfer of Control.

(7) *Non-cooperation under § 108.1810(h).* You fail to take appropriate steps, satisfactory to SBA, to accomplish any action SBA may have required under paragraph (h) of this section.

(8) *Non-notification of Events of Default.* You fail to notify SBA as soon as you know or reasonably should have known that any event of default exists under this section.

(9) *Non-notification of defaults to others.* You fail to notify SBA in writing within ten days from the date of a declaration of an event of default or nonperformance under any note, debenture or indebtedness of yours, issued to or held by anyone other than SBA.

(e) *SBA remedies for events of default with notice.* Upon written notice to you of the occurrence (as determined by SBA) of one or more of the events in paragraph (d) of this section:

(1) SBA may declare the entire indebtedness evidenced by your Debentures, including accrued interest and/or any other amounts owed SBA with respect to your Debentures, immediately due and payable: and

(2) SBA may avail itself of any remedy available under the Act, specifically including institution of proceedings for the appointment of SBA or its designee as your receiver under section 363 (c) of the Act.

(f) *Events of default with opportunity to cure.* For any occurrence (as determined by SBA) of one or more of the events in this paragraph (f), SBA may avail itself of one or more of the remedies in paragraph (g) of this section.

(1) *Excessive Management Expenses.* Without the prior written consent of SBA, you incur Management Expenses in excess of those permitted under §§ 108.510 and 108.520.

(2) *Improper Distributions.* You make any Distribution to your shareholders or partners, except with the prior written consent of SBA, other than:

(i) Distributions permitted under § 108.585; and

(ii) Payments from Retained Earnings Available for Distribution based on either the shareholders' or members' pro-rata interests or the provisions for profit distributions in your partnership agreement, as appropriate.

(3) *Failure to make payment.* Unless otherwise approved by SBA, you fail to make timely payment of any amount due under any security or obligation of yours that is issued to, held or guaranteed by SBA.

(4) *Failure to maintain Regulatory Capital.* You fail to maintain the minimum Regulatory Capital required under these regulations or, without the prior written consent of SBA, you reduce your Regulatory Capital except as permitted by § 108.585.

(5) *Capital Impairment.* You have a condition of Capital Impairment as determined under § 108.1830.

(6) *Cross-default.* An obligation of yours that is greater than $100,000 becomes due or payable (with or without notice) before its stated maturity date, for any reason including your failure to pay any amount when due. This provision does not apply if you pay the amount due within any applicable grace period or contest the payment of the obligation in good faith by appropriate proceedings.

(7) *Nonperformance.* You violate or fail to perform one or more of the terms and conditions of any security or obligation of yours that is issued to, held or guaranteed by SBA, or of any agreement (including your Participation Agreement) with or conditions imposed by SBA in its administration of the Act and the regulations promulgated under the Act.

(8) *Noncompliance.* Except as otherwise provided in paragraph (d) (5) of this section, SBA determines that you have violated one or more of the substantive provisions of the Act or any substantive regulation promulgated under the Act.

(9) *Failure to maintain diversity.* You fail to maintain diversity between management and ownership as required by § 108.150.

(g) *SBA remedies for events of default with opportunity to cure.* (1) Upon written notice to you of the occurrence (as determined by SBA) of one or more of the events of default in paragraph (f) of this section, and subject to the conditions in paragraph (g)(2) of this section:

(i) SBA may declare the entire indebtedness evidenced by your Debentures, including accrued interest, and/or any other amounts owed SBA with respect to your Debentures, immediately due and payable; and

(ii) SBA may avail itself of any remedy available under the Act, specifically including institution of proceedings for the appointment of SBA or its designee as your receiver under section 363(c) of the Act.

(2) SBA may invoke the remedies in paragraph (g)(1) of this section only if:

(i) It has given you at least 15 days to cure the default(s); and

(ii) You fail to cure the default(s) to SBA's satisfaction within the allotted time.

(h) *Repeated non-substantive violations.* If you repeatedly fail to comply with one or more of the non-substantive provisions of the Act or any non-substantive regulation promulgated under the Act, SBA, after written notification to you and until you cure such condition to SBA's satisfaction, may deny you additional Leverage and/or require you to take such actions as SBA may determine to be appropriate under the circumstances.

(i) *Consent to removal of officers, directors, or general partners and/or appointment of receiver.* The Articles of each NMVC Company must include the following provisions as a condition to the purchase or guarantee by SBA of Leverage. Upon the occurrence of any of the events specified in paragraphs (d)(1) through (d)(6) or (f)(1) through (f)(3) of this section as determined by SBA, SBA shall have the right, and you consent to SBA's exercise of such right:

(1) With respect to a Corporate NMVC Company, upon written notice, to require you to replace, with individuals approved by SBA, one or more of your officers and/or such number of directors of your board of directors as is sufficient to constitute a majority of such board; or

(2) With respect to a Partnership NMVC Company or an LLC NMVC Company, upon written notice, to require you to remove the person(s) responsible for such occurrence and/or to remove the general partner or manager of the NMVC Company, which general partner or manager shall then be replaced in accordance with NMVC Company's Articles by a new general partner or manager approved by SBA; and/or

(3) With respect to a Corporate or Partnership or LLC NMVC Company, to obtain the appointment of SBA or its designee as your receiver under section 363(c) of the Act for the purpose of continuing your operations. The appointment of a receiver to liquidate a NMVC Company is not within such consent, but is governed instead by the relevant provisions of the Act.

Computation of NMVC Company's Capital Impairment

§ 108.1830 NMVC Company's Capital Impairment definition and general requirements.

(a) *Significance of Capital Impairment condition.* If you have a condition of Capital Impairment, you are not in compliance with the terms of your Leverage. As a result, SBA has the right to impose the applicable remedies for noncompliance in § 108.1810(g).

(b) *Definition of Capital Impairment condition.* You have a condition of Capital Impairment if your Capital Impairment Percentage, as computed in § 108.1840, exceeds 70 percent.

(c) *Quarterly computation requirement and procedure.* You must determine whether you have a condition of Capital Impairment as of the end of each fiscal quarter. You must notify SBA promptly if you are capitally impaired.

(d) *SBA's right to determine NMVC Company's Capital Impairment condition.* SBA may make its own determination of your Capital Impairment condition at any time.

§ 108.1840 Computation of NMVC Company's Capital Impairment Percentage.

(a) *General.* This section contains the procedures you must use to determine your Capital Impairment Percentage. You must compare your Capital Impairment Percentage to the maximum permitted under § 108.1830(b) to determine whether you have a condition of Capital Impairment.

(b) *Preliminary impairment test.* If you satisfy the preliminary impairment test, your Capital Impairment Percentage is zero and you do not have to perform any more procedures in this § 108.1840. Otherwise, you must continue with paragraph (c) of this section. You satisfy the test if the following amounts are both zero or greater:

(1) The sum of Undistributed Net Realized Earnings, as reported on SBA Form 468, and Includible Non-Cash Gains.

(2) Unrealized Gain (Loss) on Securities Held.

(c) *How to compute your Capital Impairment Percentage.* (1) If you have an Unrealized Gain on Securities Held, compute your Adjusted Unrealized Gain using paragraph (d) of this section. If you have an Unrealized Loss on Securities Held, continue with paragraph (c)(2) of this section.

(2) Add together your Undistributed Net Realized Earnings, your Includible Non-cash Gains, and either your Unrealized Loss on Securities Held or your Adjusted Unrealized Gain.

(3) If the sum in paragraph (c)(2) of this section is zero or greater, your Capital Impairment Percentage is zero.

(4) If the sum in paragraph (c)(2) of this section is less than zero, drop the negative sign, divide by your Regulatory Capital (excluding Treasury Stock), and multiply by 100. The result is your Capital Impairment Percentage.

(d) *How to compute your Adjusted Unrealized Gain.* (1) Subtract Unrealized Depreciation from Unrealized Appreciation. This is your ''Net Appreciation''.

(2) Determine your Unrealized Appreciation on Publicly Traded and Marketable securities. This is your ''Class I Appreciation''.

(3) Determine your Unrealized Appreciation on securities that are not Publicly Traded and Marketable and

meet the following criteria, which must be substantiated to the satisfaction of SBA (this is your ''Class 2 Appreciation''):

(i) The Small Business that issued the security received a significant subsequent equity financing by an investor whose objectives were not primarily strategic and at a price that conclusively supports the Unrealized Appreciation;

(ii) Such financing represents a substantial investment in the form of an arm's length transaction by a sophisticated new investor in the issuer's securities; and

(iii) Such financing occurred within 24 months of the date of the Capital Impairment computation, or the Small Business' pre-tax cash flow from operations for its most recent fiscal year was at least 10 percent of the Small Business' average contributed capital for such fiscal year.

(4) Perform the appropriate computation from the table in § 107.1840(d)(4) of this chapter.

(5) Reduce the gain computed in paragraph (d) (4) of this section by your estimate of related future income tax expense. Subject to any adjustment required by paragraph (d)(6) of this section, the result is your Adjusted Unrealized Gain for use in paragraph (c)(2) of this section.

(6) If any securities that are the source of either Class 1 or Class 2 Appreciation are pledged or encumbered in any way, you must reduce the Adjusted Unrealized Gain computed in paragraph (d)(5) of this section by the amount of the related borrowing or other obligation, up to the amount of the Unrealized Appreciation on the securities.

Subpart L—Ending Operations as a NMVC Company

§ 108.1900 Termination of participation as a NMVC Company.

You may not terminate your participation as a NMVC Company without SBA's prior written approval. Your request for approval must be accompanied by an offer of immediate repayment of all of your outstanding Leverage (including any prepayment penalties thereon), or by a plan satisfactory to SBA for the orderly liquidation of the NMVC Company.

Subpart M—Miscellaneous

§ 108.1910 Non-waiver of SBA's rights or terms of Leverage security.

SBA's failure to exercise or delay in exercising any right or remedy under the Act or the regulations in this part does not constitute a waiver of such right or remedy. SBA's failure to require you to perform any term or provision of your Leverage does not affect SBA's right to enforce such term or provision. Similarly, SBA's waiver of, or failure to enforce, any term or provision of your Leverage or of any event or condition set forth in § 108.1810 does not constitute a waiver of any succeeding breach of such term or provision or condition.

§ 108.1920 NMVC Company's application for exemption from a regulation in this part 108.

(a) *General.* You may file an application in writing with SBA to have a proposed action exempted from any procedural or substantive requirement, restriction, or prohibition to which it is subject under this part, unless the provision is mandated by the Act. SBA may grant an exemption for such applicant, conditionally or unconditionally, provided the exemption would not be contrary to the purposes of the Act.

(b) *Contents of application.* Your application must be accompanied by supporting evidence that demonstrates to SBA's satisfaction that:

(1) The proposed action is fair and equitable; and

(2) The exemption requested is reasonably calculated to advance the best interests of the NMVC program in a manner consistent with the policy objectives of the Act and the regulations in this part.

§ 108.1930 Effect of changes in this part 108 on transactions previously consummated.

The legality of a transaction covered by the regulations in this part is governed by the regulations in this part in effect at the time the transaction was consummated, regardless of later changes. Nothing in this part bars SBA enforcement action with respect to any transaction consummated in violation of provisions applicable at the time, but no longer in effect.

§ 108.1940 Procedures for designation of additional Low-Income Geographic Areas.

(a) *General.* On its own initiative or upon written request by a Person which addresses the relevant factor(s) set forth in paragraph (b) of this section, SBA may consider whether to designate additional census tracts (or equivalent county divisions) as LI Areas.

(b) *Criteria.* SBA will consider one or more of the following factors in determining whether to designate a particular census tract (or equivalent county division) as an additional LI Area:

(1) A substantial number of Low-Income Individuals reside in that census tract (or equivalent county division).

(2) As adequately supported by studies or other analyses or reliable data, that census tract (or equivalent county division) has a pattern of unmet needs for investment capital.

(3) As adequately supported by studies or other analyses or reliable data, that census tract (or equivalent county division) has indications of economic distress.

(c) *Procedure for designation.* (1) If SBA decides to consider the designation of an additional LI Area, SBA will publish in the **Federal Register** a notice that it is considering such designation. SBA will advise the public that it will consider any comments supporting or opposing the designation, submitted within a specified time period.

(2) In making a final decision on whether to designate a particular census tract (or equivalent county division) as an additional LI Area, SBA will consider evidence submitted by any requester, SBA's own research, any public comments submitted, and any other information deemed relevant by SBA.

(3) If SBA designates a particular census tract (or equivalent county division) as an additional LI Area, SBA will publish a notice in the **Federal Register** and, if appropriate, will amend this part 108 to include the additional LI Area.

Subpart N—Requirements and Procedures for Operational Assistance Grants to NMVC Companies and SSBICs

§ 108.2000 Operational Assistance Grants to NMVC Companies and SSBICs.

(a) *NMVC Companies.* Regulations governing Operational Assistance grants to NMVC Companies may be found in subparts D and E of this part 108.

(b) *SSBICs*—(1) *Notice of Funds Availability (''NOFA'').* SBA will publish a NOFA in the **Federal Register**, advising SSBICs of the availability of funds for Operational Assistance grants to SSBICs. This NOFA will be the same as the NOFA described in § 108.300(a), or will be published simultaneously with that NOFA. An SSBIC may submit an application for an Operational Assistance grant only during the time period specified for such purpose in the NOFA.

(2) *Eligibility.* An SSBIC is eligible to apply for an Operational Assistance grant if:

(i) It intends to increase its Regulatory Capital, as in effect on December 21, 2000, and to make Developmental

Venture Capital investments in the amount of such increase;

(ii) It intends to raise binding commitments for contributions in cash or in-kind, and/or to purchase an annuity, in an amount not less than 30 percent of the intended increase in its Regulatory Capital described in paragraph (b)(2)(i) of this section; and

(iii) It has a plan describing how it intends to use the requested grant funds to provide Operational Assistance to Smaller Enterprises in which it has made or expects to make Developmental Venture Capital investments.

(3) *Application requirements*—(i) *How to apply.* An SSBIC must apply for an Operational Assistance grant using the application packet provided by SBA. Upon receipt of an application, SBA may request clarifying or technical information on the materials submitted as part of the application.

(ii) *Grant issuance fee.* An SSBIC must pay to SBA a grant issuance fee of $5,000. An SSBIC must submit this fee in advance, at the time of application submission. If SBA does not award a grant to the SSBIC, SBA will refund this fee to the SSBIC.

(4) *Contents of Application.* Each application must contain the information specified in the application packet provided by SBA, including the following information:

(i) *Amounts.* An SSBIC must specify the amount of Operational Assistance grant funds it seeks from SBA and the amount of Regulatory Capital it intends to raise after December 21, 2000.

(ii) *Plan.* An SSBIC must submit a plan addressing the following issues:

(A) *Plan for providing Operational Assistance.* The SSBIC must describe how it plans to use its grant funds to provide Operational Assistance to Smaller Enterprises in which it will make Developmental Venture Capital investments. Its plan must address the types of Operational Assistance it proposes to provide, and how it plans to provide the Operational Assistance through the use of licensed professionals, when necessary, either from its own staff or from outside entities.

(B) *Matching resources for Operational Assistance grant.* The SSBIC must include a detailed description of how it plans to obtain binding commitments for contributions in cash or in-kind, and/or to purchase an annuity, to match the funds requested from SBA for the SSBIC's Operational Assistance grant. If it proposes to obtain commitments for cash or in-kind contributions, it also must estimate the ratio of cash to in-kind contributions (in no event may in-kind contributions exceed 50 percent of the total contributions). The SSBIC must discuss its potential sources of matching resources, the estimated timing on raising such match, and the extent of the expressions of interest to commit such match to the SSBIC.

(C) *Projected amount of investment in LI Areas.* The SSBIC must describe the amount of Developmental Venture Capital investments it intends to make.

(D) *Track record of management team in obtaining public policy results through investments.* The SSBIC must provide information concerning the past track record of the SSBIC in making investments that have had a demonstrable impact on the socially or economically disadvantaged businesses targeted by the SSBIC program (for example, new businesses created, jobs created, or wealth created). Such information might include case studies or examples of the SSBIC's successful Financings.

(E) *Market analysis.* The SSBIC must provide an analysis of the LI Areas in which it intends to makes its Developmental Venture Capital investments and provide its Operational Assistance to Smaller Enterprises, demonstrating that the SSBIC understands the market and the unmet capital needs in such areas and how its activities will meet these unmet capital needs through Developmental Venture Capital investments and have a positive economic impact on those areas. The analysis must include a description of the extent of the economic distress in the identified LI Areas. The SSBIC also must analyze the extent of the demand in such areas for Developmental Venture Capital investments and any factors or trends that may affect the SSBIC's ability to make effective Developmental Venture Capital investments.

(F) *Regulatory Capital.* The SSBIC must include a detailed description of how it plans to raise its Regulatory Capital. The SSBIC must discuss its potential sources of Regulatory Capital, the estimated timing on raising such funds, and the extent of the expressions of interest to commit such funds to the SSBIC.

(G) *Projected impact.* The SSBIC must describe the criteria and economic measurements to be used to evaluate whether and to what extent it has met the objectives of the NMVC program. It must include:

(*1*) An estimate of the social, economic, and community development benefits to be created within identified LI Areas over the next five years or more as a result of its activities;

(*2*) A description of the criteria to be used to measure the benefits created as a result of its activities;

(*3*) A discussion about the amount of such benefits created that it will consider to constitute successfully meeting the objectives of the NMVC program.

(5) *Evaluation and selection.* SBA's evaluation and selection process is intended to ensure that SSBIC requests are evaluated on a competitive basis and in a fair and consistent manner. SBA will evaluate and select SSBICs for an Operational Assistance grant award solely at SBA's discretion, by considering the following criteria:

(i) The strength of the SSBIC's application, including the strength of its proposal to provide Operational Assistance to Smaller Enterprises in which it intends to invest;

(ii) The SSBIC's regulatory compliance status and past track record in being able to accomplish program goals through its investment activity;

(iii) The likelihood that and the time frame within which the SSBIC will be able to raise the Regulatory Capital it intends to raise and obtain the matching resources described in paragraph (b)(4)(ii)(B) of this section;

(iv) The need for Developmental Venture Capital investments in the LI Areas in which the SSBIC intends to invest;

(v) The SSBIC's demonstrated understanding of the markets in the LI Areas in which it intends to invest;

(vi) The extent to which the activities proposed by the SSBIC will promote economic development and the creation of wealth and job opportunities in the LI Areas in which it intends to invest and among individuals living in LI Areas;

(vii) The likelihood that the SSBIC will fulfill the goals described in its application and meet the objectives of the NMVC program; and

(viii) The strength of the SSBIC's application compared to applications submitted by other SSBICs intending to invest in the same or proximate LI Areas.

(6) *Grant award.* An SSBIC selected for an Operational Assistance grant award will receive a grant award only if it increases its Regulatory Capital and raises the matching resources required in § 108.2030 by a date established by SBA.

§ 108.2010 Restrictions on use of Operational Assistance grant funds.

(a) *Restrictions applicable only to SSBICs.* An SSBIC that receives an Operational Assistance grant must use both grant funds awarded by SBA and

its matching resources only to provide Operational Assistance in connection with a Low-Income Investment made by the SSBIC with Regulatory Capital raised after December 21, 2000.

(b) *Restrictions applicable to NMVC Companies and SSBICs.* A NMVC Company or a SSBIC that receives an Operational Assistance grant must not use either grant funds awarded by SBA or its matching resources for ''general and administrative expense,'' as defined in the Federal Acquisition Regulations, ''Contract Cost Principles and Procedures,'' 48 CFR 31.001.

§ 108.2020 Amount of Operational Assistance grant.

(a) *Amount of grant to NMVC Company.* NMVC Companies are eligible for an Operational Assistance grant award equal to the amount of matching resources raised by the NMVC Company in accordance with §§ 108.380(a)(1)(i)(B) and 108.2030.

(b) *Amount of grant to SSBIC.* SSBICs are eligible for an Operational Assistance grant award equal to the amount of matching resources raised by the SSBIC in accordance with §§ 108.2000 and 108.2030.

(c) *Pro rata reductions.* In the event that the total amount of funds available to SBA for purposes of making Operational Assistance grant awards to NMVC Companies and SSBICs is not sufficient to award grants in the amounts described in paragraphs (a) and (b) of this section, SBA will make pro rata reductions in the amounts otherwise awarded to each such NMVC Company and SSBIC.

§ 108.2030 Matching requirements.

(a) *General.* All Operational Assistance grant funds SBA awards to an NMVC Company or a SSBIC must be matched on a dollar for dollar basis with funds or other resources raised by the NMVC Company or SSBIC.

(b) *Allowable sources.* (1) Any source other than SBA is an allowable source of matching resources for an Operational Assistance grant award.

(2) Neither a NMVC Company nor a SSBIC may use funds or other resources that it has used to satisfy a legal requirement for obtaining funds under any other Federal program, to satisfy the matching resources requirements described in this part 108.

(3) A portion of Private Capital may be designated as matching resources if the designated funds are used to purchase an annuity pursuant to paragraph (c)(2)(iv) of this section or are otherwise segregated in a manner acceptable to SBA.

(c) *Type and form of matching resources.* (1) Matching resources may come from cash contributions or in-kind contributions. In-kind contributions cannot exceed 50 percent of the total amount of match raised by the NMVC Company or SSBIC.

(2) Matching resources may be in the form of:

(i) Cash,

(ii) In-kind contributions,

(iii) Binding commitments for cash or in-kind contributions that may be payable over a multiyear period acceptable to SBA (but not to exceed five years), and/or

(iv) An annuity, purchased with funds other than Regulatory Capital, from an insurance company acceptable to SBA and that may be payable over a multiyear period acceptable to SBA (but not to exceed five years).

(d) *Amount of matching resources*—(1) *NMVC Companies.* The amount of matching resources required of an NMVC Company is set forth in § 108.380(a)(1)(i)(B).

(2) *SSBICs.* The amount of matching resources required of an SSBIC is 30 percent of the increase in its Regulatory Capital since December 21, 2000, with which it has made or will make Low-Income Investments.

§ 108.2040 Reporting and recordkeeping requirements.

(a) *NMVC Companies.* Policies governing reporting, record retention, and recordkeeping requirements applicable to NMVC Companies may be found in subpart H of this part 108.

(b) *SSBICs.* An SSBIC receiving an Operational Assistance grant award must comply with all reporting, record retention and recordkeeping requirements set forth in Circular A–110 of the Office of Management and Budget and any grant award document executed between SBA and the SSBIC, as well as the reporting requirements in § 108.630(f) and the filing requirement in § 108.640.

Dated: April 16, 2001.

John Whitmore,

Acting Administrator.

[FR Doc. 01–9839 Filed 4–20–01; 8:45 am]

BILLING CODE 8025–01–P