

**CALIFORNIA CAPITAL ACCESS
PROGRAM
Amendment of Regulations
May 28, 2008**

Information Item

**STAFF SUMMARY-CPCFA
Prepared by: Aaron Todd**

ISSUE: This item is being presented to the Board for informational purposes. At the December 18, 2007 Board Meeting the Authority approved the amending of the existing regulations for the CalCAP Program. Subsequently, both emergency and permanent rulemaking packages were filed with the Office of Administrative Law (OAL). Staff has completed the public comment period for the regulations and anticipates submitting the permanent rulemaking file with OAL on Friday May 30, 2008. Staff expects that the regulations will become permanent by the end of July 2008.

BACKGROUND:

Business Model. The CalCAP Program is designed to encourage lending to small businesses that might otherwise be outside the normal underwriting criteria of participating lenders. To accomplish this, CalCAP established a loan loss reserve account in which borrowers and lenders are required to deposit a combined 4%-7% of the loan proceeds. CalCAP then matches the combined contribution of the borrower and lender and deposits these funds into the loan loss reserve account. If an enrolled loan does not perform, the lender can file a claim and recover its loss from the loan loss reserve account.

Need for regulation changes. As the popularity and success of the CalCAP program has grown, the number of Participating Financial Institutions enrolled in the program increases. During 2007 alone, seven new banks joined; which ultimately results in more strain on CPCFA funds to cover CalCAP costs. The changes to the regulations are designed to (1) refocus CalCAP on truly small businesses in order to provide maximum return for the limited resources, and (2) clarify several items. The amendments to the existing regulations are the result of preliminary conversations with lenders and staff recommendations.

SUMMARY OF CHANGES:

The proposed amendments were enacted by way of the emergency regulation process on January 23, 2008. Since this date CalCAP has been operating with the following changes outlined below.

Substantive Regulation Changes

- 1. Revised definition of “Independent Contributor” to include fees also paid by the lender.** This change allows Independent Contributors, such as other State Agencies, to make the lender’s contribution to the loan loss reserve account.

Current regulations allow Independent Contributors to pay the Authority's premium and the Borrower's fees. *Section 8070 (f)*.

2. **Revised definition of "Small Business Concern" so that a "Small Business Concern" will be defined as a business with 100 employees or less and average revenues for the previous three years that do not exceed \$10,000,000.** This changed the definition of small business from 500 or less employees to 100 or less and revenues not to exceed \$10,000,000. The revised definition mirrors the small business definition used by DGS for procurement of goods and services. We estimate this change will save the Authority approximately \$750,000 annually. *Section 8070 (v)*.
3. **Revised the regulations so that the maximum combined dollar amount of qualified loans any one borrower can receive is \$1,500,000 over three years for all lenders. Additionally, the revised regulations require the borrower to certify it does not have CalCAP loans outstanding in excess of \$1,500,000 and require lenders to pre-qualify all loans that are \$500,000 or more.** Previous regulations allowed a borrower to receive up to 2,500,000 per lender. We initially proposed a \$1,000,000 cap but revised this up to \$1,500,000 based on lender feedback. We estimate this change will result in approximately \$350,000 in savings annually. *Section 8072(c) (21) (24) and Section 8072 (e) (9)*.
4. **Added the requirement that the borrower has certified it has applied and/or secured all applicable licenses and/or permits to conduct the business activity.** Previous CalCAP regulations do not have any such requirement. Many of the loans in the CalCAP portfolio are for businesses that require licenses such as daycare centers, insurance agents, chiropractors, etc. *Section 8072(c) (24)*.
5. **Revised the regulations so that interest earnings on any loan loss reserve account have a minimum interest rate comparable to the market rate for an account of similar size.** Previous regulations did not have any such requirement. Some lenders pay as low as 0.25% on the CalCAP loan loss reserve accounts they maintain. *Section 8073(c)*.

Clarifying Regulation Changes

1. **Revised the definition of "Financial Institution" to include language requiring that "Financial Institutions" maintain an office in California.** Previous regulations did not have any such requirement. This revision is necessary as CalCAP staff have received several inquiries from out of state lenders interested in participating in the program. *Section 8070 (e) (3)*.
2. **Revised the definition of "Matching Contribution" so that "Matching Contribution" will now be defined "as set forth in Health and Safety Code Section 44559.4(d)(1)." *Section 8070 (j)*.**

3. **Revised the definition of “Qualified Loan” to include language that a “Qualified Loan” is any portion of a loan not already enrolled in another governmental guarantee program.** Previous regulations do not have any such requirement. This practice is problematic for several reasons. First, for every one dollar loaned, two dollars in guarantees are used. Second, this practice can lead to possible “double-dipping” by a lender. *Section 8070 (s) (5) and Section 8072(c)(25).*
4. **Clarify that the Authority should be notified within 10 “Business Days” that a Qualified Loan is being enrolled in the program.** Current regulations are ambiguous. *Section 8072(b) (1).*
5. **Delete the reference to Sheshunoff Inc. and replace with Highline Inc.** Sheshunoff Inc. was a company that provided bank rating services. Sheshunoff Inc. no longer exists as it was bought out by Highline Inc. *Section 8073(c) (2).*

Attached is a redline version of the CalCAP regulations that show the amendments.

REGULATORY PROCESS: After the Authority approved the amending of the existing regulations at the December 18, 2007 Board Meeting both emergency and permanent rulemaking packages were filed with the Office of Administrative Law (OAL). After OAL review and approval, the emergency regulations went into effect January 23, 2008. On March 14, 2008 staff began the permanent rulemaking process. On March 14, 2008, the Authority prepared a “Notice of Proposed Rulemaking” which was published in the California Regulatory Notice Register, mailed to our participating financial institutions and interested persons, as well as posted the Authority’s website on March 28, 2008. The notice started the OAL 45-day public comment period. On May 12, 2008 the forty-five day public comment period on the permanent regulations was completed with no comments received. Also, on May 12, 2008, a public hearing on the permanent regulations was held here at the State Treasurer’s Office and no comments were submitted. Staff anticipates submitting the permanent rulemaking file with OAL on Friday May 30, 2008. OAL has 30 working days to review the regulations for compliance with the Administrative Procedure Act and the Authority’s statute. Once OAL approves the regulations, they are filed with the Secretary of State and become effective as permanent regulations 30 days later.

PROPOSED TEXT OF REGULATIONS

Title 4. Business Regulations

Division 11. California Pollution Control Financing Authority

Article 7. Capital Access Program for Small Businesses

Amend § 8070. Definitions.

In addition to the definitions in Section 8020, the following terms shall have the following definitions, unless the context requires otherwise:

(a) "Borrower" means a Qualified Business which obtains a Qualified Loan from a Participating Financial Institution.

(b) "Early Stage Loan" means each of the first \$500,000 of Qualified Loan made by a Participating Financial Institution.

(c) "Executive Director" means the Executive Director of the California Pollution Control Financing Authority, or his or her designee from time to time.

(d) "Fees" means a non-refundable fee, agreed to by the Participating Financial Institution and the Borrower, of no less than 2 percent and no more than 3-1/2 percent of the principal amount of the Qualified Loan which the Borrower shall be required to pay to the Participating Financial Institution for deposit in the Loss Reserve Account, together with an equal, matching amount which the Participating Financial Institution shall deposit in the Loss Reserve Account.

(e) (1) "Financial Institution" means a federal or state-chartered bank, savings association, credit union, not-for-profit community development financial institution certified under Part 1805 (commencing with Section 1805.100) of Chapter XVIII of Title 12 of the Code of Federal Regulations, or a consortium of the foregoing entities. A consortium of such entities may include a nonfinancial corporation, if the percentage of capitalization by all nonfinancial corporations in the consortium does not exceed 49 percent.

(2) "Financial Institution" also includes a lending institution that has executed a participation agreement with the Small Business Administration under the guaranteed loan program pursuant to Part 120 (commencing with Section 120.1) of Chapter 1 of Title 13 of the Code of Federal Regulations and meets the requirements of Section 120.410 of Chapter 1 of Title 13 of the Code of Federal Regulations, and a small business investment company licensed pursuant to Part 107 (commencing with Section 107.20) of Chapter 1 of Title 13 of the Code of Federal Regulations.

(3) A financial institution described in paragraph (1) shall have at least one office in the State of California.

(4) A financial institution described in paragraph (2) shall be domiciled or have its principal office in the State of California.

(f) "Independent Contributor" means any individual, company, corporation, institution, foundation, utility, government agency or other entity, including any consortium of these persons or entities, whether public or private (but excluding any Borrower), that, pursuant to the provisions of this Article, pays to a Loss Reserve Account the Matching Contribution and/or Fees payable by the Borrower and/or the Financial Institution.

(g) "Individual" means a natural person, together, if applicable, with any of his or her spouse, parents, siblings or children or the parents or spouse of any of them.

(h) "Law" means Article 8 (commencing with Section 44559) of Chapter 1 of Division 27 of the California Health and Safety Code, as amended from time to time.

(i) "Loss Reserve Account" means an account held by a Program Trustee or by any Participating Financial Institution that is established and maintained by the Authority for the benefit of a Participating Financial Institution for the purposes set forth in Section 8073.

(j) "Matching Contribution" means a contribution to a Loss Reserve Account ~~of an amount equal to~~
~~—(A) 100 percent of the combined amount of the Fees, or~~
~~—(B) 150 percent of the combined amount of the Fees for~~
~~—(1) a Qualified Loan to a Borrower in a Severely Affected Community or~~
~~—(2) an Early Stage Loan; provided, however, that such contribution shall not in any case exceed 150 percent of the combined amount of the Fees.~~ as set forth in the Health and Safety Code Section 44559.4(d)(1).

(k) "Money Market Fund" means an open-ended management investment company regulated under the Investment Company Act of 1940, as amended, which values its securities pursuant to Section 270.2a-7 of Title 17 of the Code of Federal Regulations.

(l) "Participating Financial Institution" means a Financial Institution that has been approved by the Authority to enroll Qualified Loans in the Program and has agreed to all terms and conditions set forth in the Law and this Article and as may be required by any applicable federal law providing matching funding.

(m) "Passive Real Estate Ownership" means ownership of real estate for the purpose of deriving income from speculation, trade or rental, but does not include any of the following:

(1) The ownership of that portion of real estate being used or intended to be used for the operation of the business of the owner of the real estate; or

(2) The ownership of real estate for the purpose of construction or renovation, until the completion of the construction or renovation phase.

For purposes of clause (1) above, the Borrower must be using or planning to use upon acquisition or construction of a building, at least 51 percent of the space in an existing building or at least 67 percent of the space in a newly constructed building. The requirements of clause (1) above will be deemed to be satisfied when a Participating Financial Institution makes a Qualified Loan to an Individual, or to a partnership or trust wholly owned or controlled by one or more Individuals, for the purpose of financing property that will be leased to a Qualified Business that is wholly owned by those same Individuals, and in such case the Qualified Loan will be deemed to be made also to such Qualified Business.

(n) "Primary business location in California" means that a business will be deemed to be located in California if either:

(1) a majority of the employees of the business are located in California; or

(2) the Executive Director determines that the Primary business location is in California by finding that the average of the "Payroll Factor" as defined in Revenue and Taxation Code Section 25132, the "Income Factor" as defined in Revenue and Taxation Code Section 25128, and the "Sales Factor" as defined in Revenue and Taxation Code Section 25134 is greater than 50 percent.

(o) "Primary economic effect in California" means, as applied to a business activity, that either of the following conditions exists:

(1) At least 51 percent of the total revenues of the business activity are generated in California; or

(2) At least 51 percent of the total jobs of the business activity are created or retained in California.

(p) "Program" means the Capital Access Loan Program for Small Businesses established pursuant to the Law.

(q) "Program Trustee" means a bank or trust company, or the State Treasurer, chosen by the

Authority from time to time to hold or administer some or all of the Loss Reserve Accounts.

(r) "Qualified Business" means a Small Business Concern that meets both of the following criteria:

(1) It is a corporation, partnership, cooperative, or other entity, whether that entity is a nonprofit entity or an entity established for profit, that is authorized to conduct business in California.

(2) It has its Primary business location in California.

(s) "Qualified Loan" means a loan or a portion of a loan made by a Participating Financial Institution to a Qualified Business for any business activity that has its Primary economic effect in California. A Qualified Loan may be made in the form of a line of credit, in which case the Participating Financial Institution shall specify the amount of the line of credit to be covered under the Program, which may be equal to the maximum commitment under the line of credit or an amount that is less than the maximum commitment. "Qualified Loan" does not include any of the following:

(1) A loan for the construction or purchase of residential housing.

(2) A loan to finance Passive Real Estate Ownership.

(3) A loan for the refinancing of debt already held by the Participating Financial Institution other than a prior Qualified Loan enrolled under the Program, except to the extent of any increase in the outstanding balance.

(4) A loan, the proceeds of which will be used

(A) to provide any of the following facilities: any private or commercial golf course, country club, massage parlor, tennis club, skating facility (including roller skating, skateboard, and ice skating), racquet sports facility (including any handball or racquetball court), hot tub facility, suntan facility, racetrack, airplane, skybox (or other private luxury box), health club facility, facility primarily used for gambling or to facilitate gambling, or store whose principal business is the sale of alcoholic beverages for consumption off premises, a store or other facility whose principal business is the sale of firearms, a store or other facility whose principal business is the manufacture or sale of tobacco or tobacco products, any religious facility or organization, escort service, nudist camp, gun club, shooting range or gallery; or

(B) in any manner that could cause the interest on any bonds previously issued by the Authority to become subject to federal income tax, as specified in writing to all Participating Financial Institutions by the Executive Director.

(5) any loan or portion thereof to the extent the same loan or portion thereof has been, is being, or will be enrolled in any other government program substantially similar to the Program.

(t) "Severely Affected Community" means any area classified as an enterprise zone pursuant to the Enterprise Zone Act, Chapter 12.8 (commencing at Section 7070) of Division 7 of Title 1 of the California Government Code; any area, as designated by the Executive Director, contiguous to the boundaries of a military base designated for closure pursuant to Public Law 101-150, as amended; and any other comparable economically distressed geographic area so designated by the Executive Director from time to time.

(u) "Small Business Assistance Fund" means a fund of that name created by the Authority.

(v) "Small Business Concern" means an independently owned and operated business that is not dominant in its field of operation, the principal office of which is located in California, the officers of which are domiciled in California, and that, together with affiliates, has 100 or fewer employees, and average annual gross receipts of ten million dollars (\$10,000,000) or less over the previous three years.

(w) "Standards" means the criteria, limited to geographical area and/or type of business, to be used by an Independent Contributor in selecting businesses to assist through the Program.

NOTE: Authority cited: Sections 44520 and 44559.5(f), Division 27, Health and Safety Code.

Reference: Sections 44559.1, 44559.2, 44559.3, 44559.4, 44559.5 and 44559.7, Division 27, Health and Safety Code.

HISTORY

1. New article 7 and section filed 3-21-94 as an emergency; operative 3-21-94 (Register 94, No. 12). This filing was deemed an emergency by Health and Safety Code section 44520(b). A Certificate of Compliance must be transmitted to OAL by 9-19-94 or the emergency regulation will be repealed by operation of law on the following day.
2. Certificate of Compliance as to 3-21-94 order including amendment of subsections (n)(3) and (p) and NOTE transmitted to OAL 9-16-94 and filed 10-31-94 (Register 94, No. 44).
3. Amendment of subsections (d) and (e), new subsections (f) and (g) and subsection relettering, amendment of newly designated subsection (i), new subsections (j)-(k)(2) and subsection relettering, amendment of newly designated subsections (l) and (m)(2), repealer of former subsections (m)(3)- (m)(3)(B), amendment of newly designated subsections (t)-(v), new subsection (w), and amendment of NOTE filed 2-6-96 as an emergency pursuant to Health and Safety Code section 44520(b); operative 2-6-96 (Register 96, No. 6). Pursuant to Health and Safety Code section 44520(b), a Certificate of Compliance must be transmitted to OAL by 8-5-96 or emergency language will be repealed by operation of law on the following day.
4. Certificate of Compliance as to 2-6-96 order, including amendment of subsection (d), new subsection (k), subsection relettering, and amendment of newly designated subsection (r), transmitted to OAL 8-2-96 and filed 9-10-96 (Register 96, No. 37).
5. Amendment of subsections (d), (f) and (l)(1) filed 12-23-98; operative 12-23-98 pursuant to Government Code section 11343.4(d) (Register 98, No. 52).
6. Amendment of subsections (e), (t) and (t)(4)(A) filed 2-24-2000 as an emergency pursuant to Health and Safety Code section 44520; operative 2-24-2000 (Register 2000, No. 8). A Certificate of Compliance must be transmitted to OAL by 8-22-2000 or emergency language will be repealed by operation of law on the following day.
7. Certificate of Compliance as to 2-24-2000 order transmitted to OAL 8-21-2000 and filed 10-2-2000 (Register 2000, No. 40).
8. Repealer of subsections (l)-(l)(2), subsection relettering and amendment of newly designated subsection (s)(4)(A) filed 12-18-2000 as an emergency pursuant to Health and Safety Code section 44520; operative 1-1-2001 (Register 2000, No. 51). A Certificate of Compliance must be transmitted to OAL by 7-2-2001 or emergency language will be repealed by operation of law on the following day.
9. Certificate of Compliance as to 12-18-2000 order transmitted to OAL 6-14-2001 and filed 7-26-2001 (Register 2001, No. 30).
10. Change without regulatory effect redesignating former section (e) as new subsection (e)(1) and adding subsections (e)(2)-(3) filed 10-29-2001 pursuant to section 100, title 1, California Code of Regulations (Register 2001, No. 44).

Amend § 8071. Application by Financial Institution.

(a) A Financial Institution seeking to participate in the Program will complete a registration application provided by the Authority.

The application shall include the following information:

- (1) name of applicant Financial Institution.
- (2) name, address and telephone number of contact person.
- (3) combined capital and surplus as of the end of the Financial Institution's most recent fiscal year.
- (4) number of lending branches.
- (5) certification that the applicant Financial Institution is not subject to a cease and desist order or other regulatory sanction with the appropriate federal or state regulatory body, which would impair its ability to participate in the Program, and the name of that body.
- (6) a full description of the board of directors, including number, race, ethnicity and gender of its members.
- (7) the Financial Institution's rating from a nationally recognized credit rating agency which assesses the financial soundness and stability of financial institutions.
- (8) the Financial Institution's agreement to follow the Program's procedures as set forth in the Law and this Article.
- (9) the Financial Institution's agreement to permit an audit of any of its records relating to enrolled Qualified Loans, during normal business hours on its premises, by the Authority or its agents, and to supply such other information concerning enrolled Qualified Loans as shall be requested by the Executive Director.
- (10) acknowledgment by the Financial Institution that the Authority and the State will have no liability to the Participating Financial Institution under the Program except from funds deposited in the Loss Reserve Account for the Participating Financial Institution.

(b) Upon receipt of a completed application, the Executive Director will within 10 business days review and determine whether additional information is required, or whether the application is sufficient to permit the applicant to be a Participating Financial Institution. The Executive Director's decision whether an application is sufficient shall be final.

(c) A Participating Financial Institution shall be authorized to request the Authority to establish two or more Loss Reserve Accounts for such institution, so that the institution shall be able to allocate any Qualified Loan enrolled under Section 8072 to whichever Loss Reserve Account it designates. In such case, the definition of Early Stage Loan and Section 8074(f) shall be applied in the aggregate to all the Loss Reserve Accounts for each Participating Financial Institution.

NOTE: Authority cited: Sections 44520 and 44559.5(f), Division 27, Health and Safety Code.
Reference: Section 44559.2, Division 27, Health and Safety Code.

HISTORY

1. New section filed 3-21-94 as an emergency; operative 3-21-94 (Register 94, No. 12). This filing was deemed an emergency by Health and Safety Code section 44520(b). A Certificate of Compliance must be transmitted to OAL by 9-19-94 or the emergency regulation will be repealed by operation of law on the following day.
2. Certificate of Compliance as to 3-21-94 order including amendment of NOTE transmitted to OAL 9-16-94 and filed 10-31-94 (Register 94, No. 44).
3. Amendment of subsections (a)(2), (a)(5) and (b) filed 2-6-96 as an emergency pursuant to Health and Safety Code section 44520(b); operative 2-6-96 (Register 96, No. 6). Pursuant to Health and Safety Code section 44520(b), a Certificate of Compliance must be transmitted to

OAL by 8-5-96 or emergency language will be repealed by operation of law on the following day.

4. Certificate of Compliance as to 2-6-96 order transmitted to OAL 8-2-96 and filed 9-10-96 (Register 96, No. 37).

Amend § 8072. Loan Enrollment.

(a) The terms and conditions of Qualified Loans, including interest rates, fees and other conditions, shall be determined solely by agreement of the Participating Financial Institution and the Borrower.

(b) A Participating Financial Institution shall be authorized to enroll under the Program all or a part of any Qualified Loan:

(1) by notifying the Authority in writing, within 10 business days after the Qualified Loan is made, that it is enrolling a Qualified Loan. For purposes of this section, the date on which the Participating Financial Institution makes a Qualified Loan is the date on which the Participating Financial Institution first disburses proceeds of the Qualified Loan to the Borrower; and

(2) by transmitting to the Authority the Fees collected from the Participating Financial Institution and the Borrower, or from an Independent Contributor on behalf of the Borrower and/or the Authority, in connection with the Qualified Loan, and by providing written evidence that the Fees have been deposited in a Loss Reserve Account held by either the Participating Financial Institution or the Program Trustee.

(c) The notification to the Authority shall include at least the following information:

(1) Name, D/B/A (if any), address, telephone and fax number of the Borrower.

(2) Brief description of the Borrower's business and either the SIC Code(s) or the NAICS Code(s) applicable to such business.

(3) Brief description of the Borrower's regular activities and the amount of its annual revenues.

(4) Brief summary of the intended use of the proceeds of the Qualified Loan.

(5) Amount of the Qualified Loan being enrolled (and indication if less than the full amount of the Qualified Loan is being enrolled).

(6) Type of the Qualified Loan (e.g., line of credit, term loan, equipment loan).

(7) Date of the Qualified Loan.

(8) Interest rate applicable to the Qualified Loan.

(9) Term of the Qualified Loan.

(10) Geographic location of the Qualified Business and the location of the facilities being financed if different.

(11) Whether the Qualified Business or the location of the facilities being financed is in a Severely Affected Community.

(12) Whether the loan is secured.

(13) Whether the loan is a refinancing, and if so, whether the prior loan was enrolled under the Program, and whether the amount of the loan was increased as part of the refinancing.

(14) Agreed amount of the Fees payable by each of the Borrower and the Participating Financial Institution.

(15) Whether any portion of the Fees payable by the Borrower or the Matching Contribution was or is to be paid by an Independent Contributor; the identity of such Independent Contributor; and a certification that the Independent Contributor has approved the use of its funds to pay such Fees or Matching Contribution in connection with the Qualified Loan.

(16) Number of persons currently employed by the Borrower, and number of jobs expected to

be created, retained or affected by the Qualified Loan.

(17) Certification that the loan is a Qualified Loan, and that the business receiving the Qualified Loan is a Qualified Business.

(18) Certification that the Qualified Loan is for a business activity that has its Primary economic effect in California.

(19) Certification that, upon request of the Executive Director, the Participating Financial Institution will provide information from the financial records of the Borrower, and that the Participating Financial Institution has obtained the consent of the Borrower to such disclosure.

(20) Certification that the Participating Financial Institution has obtained a written representation from the Borrower that it has no legal, beneficial or equitable interest in the Fees or the Matching Contribution.

(21) Certification that the aggregate principal amount of the loan, together with all other Qualified Loans made by any Participating Financial Institution under the Program to the Borrower over the last three years (including all related entities among which a common enterprise exists), does not exceed \$1,500,000.

(22) Certification that the Participating Financial Institution has notified the Borrower if the Participating Financial Institution's share of the Fees for the Qualified Loan have been paid from loan proceeds.

(23) Acknowledgment that the lending activities of the Participating Financial Institution are subject to safety and soundness standards as set forth in applicable federal banking regulations. The Participating Financial Institution shall be authorized to base the information requested by subsections (4), (16), (17) (18) and (21) above upon representations made to it by the Borrower; provided that no such Borrower representation may be relied upon if it is known to be false by the lending officer(s) at the Participating Financial Institution who are directly involved in the negotiation of the Qualified Loan.

(24) Certification that the Participating Financial Institution has obtained a written representation from the Borrower that it has secured or made application for all applicable licenses or permits needed to conduct its business.

(25) Certification from the Participating Financial Institution that it has not, and will not, enroll the same loan or portion thereof in any other government program substantially similar to the Program.

(26) Certification that the Borrower does not meet the Participating Financial Institution's normal underwriting criteria for making loans of the type sought to be enrolled and that without enrollment, the Participating Financial Institution would not make the loan.

(d) If a Borrower seeking a loan from a Participating Financial Institution has less than a majority of its employees in California, the Participating Financial Institution shall be authorized to submit information to, and seek a determination from, the Executive Director that such Borrower has its Primary business location in California. Such determination shall be made by the Executive Director within 10 days of receipt of a written request from a Participating Financial Institution containing information about the business activities of the proposed Borrower.

(e) If a Borrower seeking a Qualified Loan from a Participating Financial Institution is an employee, member, director, officer, principle shareholder, or affiliate of the Participating Financial Institution, the terms and the conditions of the Qualified Loan and the internal procedures used to approve the Qualified Loan must comply with the following requirements:

(1) If the Participating Financial Institution is a federal-chartered bank, the Qualified Loan

must be made in accordance with all applicable federal banking laws that regulate conflicts of interests and insider transactions and Sections 371c, 371c-1, 375a, and 375b of the Title 12 of the United States Code, and Sections 215.4 of Title 12 of the Code of Federal Regulations.

(2) If the Participating Financial Institution is a state-chartered bank, the Qualified Loan must be made in accordance with all applicable state banking laws that regulate conflicts of interests and insider transactions and Section 3370 et seq. of the Financial Code, and Article 8, Title 10, of the California Code of Regulations.

(3) If the Participating Financial Institution is a federal-chartered savings association, the Qualified Loan must be made in accordance with all applicable federal banking laws that regulate conflicts of interests and insider transactions and Section 1468 of Title 12 of the United States Code.

(4) If the Participating Financial Institution is a state-chartered savings association, the Qualified Loan must be made in accordance with all applicable state banking laws that regulate conflicts of interests and insider transactions and Sections 6503 and 6529 of the Financial Code.

(5) If the Participating Financial Institution is a federal-chartered credit union, the Qualified Loan must be made in accordance with all applicable federal banking laws that regulate conflicts of interests and insider transactions and Sections 1757 and 1761c of Title 12 of the United States Code and Section 701.21(d) of Title 12 of the Code of Federal Regulations.

(6) If the Participating Financial Institution is a state-chartered credit union, the Qualified Loan must be made in accordance with all applicable state banking laws that regulate conflicts of interests and insider transactions and Section 15050 of the Financial Code.

(7) If the Participating Financial Institution is a not-for-profit certified community development financial institution (CDFI), the Qualified Loan must be made in accordance with all applicable federal banking laws that regulate conflicts of interests and insider transactions and Section 1805.807 of Title 12 of the Code of Federal Regulations.

(8) If the Participating Financial Institution is a lending institution as described in Section 44559.1(d)(2) of the Health and Safety Code, the Qualified Loan must be made in accordance with all applicable federal laws that regulate conflicts of interests and insider transactions and Section 120.140 of Title 12 of the Code of Federal Regulations.

(9) The Participating Financial Institution shall pre-qualify with the Authority any qualified loan with a principal amount of \$500,000 or more.

(f) The Authority shall, upon receipt of documentation and Fees from the Participating Financial Institution, enroll the Qualified Loan if the Executive Director determines that the Qualified Loan meets the requirements of the Law and this Article. The Executive Director shall notify the Participating Financial Institution of enrollment within 10 days after receipt by the Authority of all documentation and Fees required by the Law and/or this Article. The Executive Director's determination whether a loan shall be enrolled in the Program shall be final. The Executive Director shall be authorized to review an application for enrollment submitted by a Participating Financial Institution in advance of the making of the loan, and notify the institution whether such loan meets the requirements of the Law and this Article.

(g) Upon enrollment of a Qualified Loan, the Matching Contribution shall be transferred for deposit in the Loss Reserve Account (1) by the Authority or (2) by an Independent Contributor, and the Program Trustee shall notify the Participating Financial Institution of the transfer and of the source of funds from which the transfer was made.

(h) The Participating Financial Institution shall notify the Authority within 60 days after any extension or renewal of any enrolled loan which does not increase the loan amount. If the

amount is increased, a new loan enrollment form shall be submitted within such time, and Fees shall be transmitted or deposited pursuant to Section 8072(b)(2) based on the increased amount.

(i) The Participating Financial Institution shall notify the Authority of the work-out status on Qualified Loans for which extension/renewal or charge off status is not yet clear. The "Notification of Work-Out Status" form provided by the Authority shall be used to notify the Authority. The Participating Financial Institution shall have up to 240 days from such initial notification to inform the Authority of re-enrollment or charge off.

NOTE: Authority cited: Sections 44520 and 44559.5(f), Division 27, Health and Safety Code.
Reference: Sections 44559.2 and 44559.4, Division 27, Health and Safety Code.

HISTORY

1. New section filed 3-21-94 as an emergency; operative 3-21-94 (Register 94, No. 12). This filing was deemed an emergency by Health and Safety Code section 44520(b). A Certificate of Compliance must be transmitted to OAL by 9-19-94 or the emergency regulation will be repealed by operation of law on the following day.
2. Certificate of Compliance as to 3-21-94 order including amendment of subsection (c)(20), new subsections (g) and (h) and amendment of NOTE transmitted to OAL 9-16-94 and filed 10-31-94 (Register 94, No. 44).
3. Amendment of subsections (b)(1), (b)(2) and (c)(2), new subsections (c)(3) and (c)(4) and subsection renumbering, amendment of newly designated subsection (c)(6), new subsections (c)(8) and (c)(9), amendment of newly designated subsections (c)(11) and (c)(14), new subsection (c)(15), amendment of newly designated subsections (c)(16), (c)(17), (c)(19) and (c)(22), amendment of subsections (d) and (e), new subsection (f) and subsection relettering, and amendment of newly designated subsections (g) and (h) filed 2-6-96 as an emergency pursuant to Health and Safety Code section 44520(b); operative 2-6-96 (Register 96, No. 6). Pursuant to Health and Safety Code section 44520(b), a Certificate of Compliance must be transmitted to OAL by 8-5-96 or emergency language will be repealed by operation of law on the following day.
4. Certificate of Compliance as to 2-6-96 order, including amendment of subsections (c)(4), (c)(15), (c)(17) and (c)(22), and new subsections (c)(23)- (24), transmitted to OAL 8-2-96 and filed 9-10-96 (Register 96, No. 37).
5. Amendment of subsections (a), (b)(2), (c)(2), (c)(3), (c)(15), (c)(19), (c)(22), (d), (e), (h) and (i) filed 12-23-98; operative 12-23-98 pursuant to Government Code section 11343.4(d) (Register 98, No. 52).
6. Amendment of subsections (c)(1)-(3), (c)(19) and (c)(21) filed 2-24-2000 as an emergency pursuant to Health and Safety Code section 44520; operative 2-24-2000 (Register 2000, No. 8). A Certificate of Compliance must be transmitted to OAL by 8-22-2000 or emergency language will be repealed by operation of law on the following day.
7. Certificate of Compliance as to 2-24-2000 order transmitted to OAL 8-21-2000 and filed 10-2-2000 (Register 2000, No. 40).
8. Repealer of subsection (c)(19), subsection renumbering, amendment of newly designated subsection (c)(23) and subsection (d), repealer of subsection (f), subsection relettering and amendment of NOTE filed 12-18-2000 as an emergency pursuant to Health and Safety Code section 44520; operative 1-1-2001 (Register 2000, No. 51). A Certificate of Compliance must be transmitted to OAL by 7-2-2001 or emergency language will be repealed by operation of law on the following day.

9. Certificate of Compliance as to 12-18-2000 order transmitted to OAL 6-14-2001 and filed 7-26-2001 (Register 2001, No. 30).
10. Amendment of subsections (b)(1) and (g) filed 8-8-2002 as an emergency pursuant to Health and Safety Code section 44520(b); operative 8-8-2002 (Register 2002, No. 32). A Certificate of Compliance must be transmitted to OAL by 2-4-2003 or emergency language will be repealed by operation of law on the following day.
11. Certificate of Compliance as to 8-8-2002 order transmitted to OAL 2-3-2003 and filed 3-6-2003 (Register 2003, No. 10).

Amend § 8073. Loss Reserve Accounts.

(a) Upon the Executive Director's acceptance of an application under Section 8071, the Authority shall establish a Loss Reserve Account for that Participating Financial Institution for the following purposes:

- (1) to receive all Fees deposited by the Participating Financial Institution, Borrowers and/or Independent Contributors;
- (2) to receive Matching Contributions deposited by the Authority and/or Independent Contributors; and
- (3) to pay claims in accordance with Section 8074.

(b) The Loss Reserve Account shall, in the Authority's sole determination, be held by the Participating Financial Institution or by a Program Trustee.

(c) Any Loss Reserve Account held in a Participating Financial Institution shall be an interest-bearing demand account or deposit account at a banking institution, or a Money Market Fund approved by the Executive Director, or a combination thereof, and earning a rate of interest that would be expected of accounts of similar type and size. The Loss Reserve Account shall be insured by the Federal Deposit Insurance Corporation, the National Credit Union Share Insurance Fund, or the Securities Investor Protection Corporation, as appropriate, to the extent permitted by law. The Authority shall not deposit any Loss Reserve Account with a Participating Financial Institution if:

- (1) there are any charges by the Participating Financial Institution for the establishment or maintenance of the Loss Reserve Account at such Financial Institution; or
- (2) at the time the Loss Reserve Account is established with the Participating Financial Institution, it has a rating below "75" from IDC Financial Publishing Inc.'s Bank Financial Quarterly, S&L-Savings Bank Financial Quarterly, or Credit Union Financial Profiles, or it has a rating below "11" from Highline Inc.'s Bank Quarterly or S&L Quarterly or successor publication approved by the Executive Director.

(d) All moneys in a Loss Reserve Account are property of the Authority (subject to the Participating Financial Institution's right to receive a portion of the remaining balance in the Loss Reserve Account upon its withdrawal from the Program pursuant to Section 8076 and subject to subsection (e) below). Interest or income earned on moneys credited to the Loss Reserve Account shall be deemed to be part of the Loss Reserve Account. The Executive Director shall be authorized to withdraw moneys from the Loss Reserve Account to offset administrative costs associated with the Program, provided that the Executive Director shall not be authorized to withdraw more than 50 percent of all interest or income credited to the Loss Reserve Account. The Executive Director shall be authorized to return to a Participating Financial Institution any fees improperly deposited in a Loss Reserve Account.

(e) Notwithstanding any other provision of this article, the Executive Director shall be

authorized, with the approval of the applicable Participating Financial Institution, to assign, transfer, pledge or create security interests in all or a portion of any Loss Reserve Account to any other entity or entities (including a trustee of a securitization trust or trusts) in connection with the securitization of all or a portion of the Participating Financial Institution's loans enrolled in the Program.

NOTE: Authority cited: Sections 44520 and 44559.5(f), Division 27, Health and Safety Code.
Reference: Sections 44559.3 and 44559.8, Division 27, Health and Safety Code.

HISTORY

1. New section filed 3-21-94 as an emergency; operative 3-21-94 (Register 94, No. 12). This filing was deemed an emergency by Health and Safety Code section 44520(b). A Certificate of Compliance must be transmitted to OAL by 9-19-94 or the emergency regulation will be repealed by operation of law on the following day.
2. Certificate of Compliance as to 3-21-94 order including amendment of subsections (a) and (d) and NOTE transmitted to OAL 9-16-94 and filed 10-31-94 (Register 94, No. 44).
3. Amendment of subsections (a)(1) and (2), (b) and (d) filed 2-6-96 as an emergency pursuant to Health and Safety Code section 44520(b); operative 2-6-96 (Register 96, No. 6). Pursuant to Health and Safety Code section 44520(b), a Certificate of Compliance must be transmitted to OAL by 8-5-96 or emergency language will be repealed by operation of law on the following day.
4. Certificate of Compliance as to 2-6-96 order, including amendment of subsections (c)-(c)(1), transmitted to OAL 8-2-96 and filed 9-10-96 (Register 96, No. 37).
5. Amendment of subsections (c) and (d) filed 12-23-98; operative 12-23-98 pursuant to Government Code section 11343.4(d) (Register 98, No. 52).
6. Amendment of subsection (d), new subsection (e) and amendment of NOTE filed 2-24-2000 as an emergency pursuant to Health and Safety Code section 44520; operative 2-24-2000 (Register 2000, No. 8). A Certificate of Compliance must be transmitted to OAL by 8-22-2000 or emergency language will be repealed by operation of law on the following day.
7. Certificate of Compliance as to 2-24-2000 order transmitted to OAL 8-21-2000 and filed 10-2-2000 (Register 2000, No. 40).