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## Legislation Enacted to Create the Small Business Lending Fund

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Banking & Credit Unions; Financial Services

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On September 27, 2010, the President signed the "Small Business Jobs and Credit Act of 2010," which is intended to provide additional support for small business lending in the wake of the recent financial crisis. Among other things, the legislation creates a \$30 billion "Small Business Lending Fund" (Fund) that the Department of Treasury (Treasury) may use to make capital investments in eligible depository institutions to facilitate small business lending. Significantly, the legislation authorizes eligible institutions to use the Fund to refinance securities that have been issued to Treasury under the TARP Capital Purchase Program.

The Fund is available to institutions with less than \$10 billion in assets as of December 31, 2009. Holding companies with less than \$10 billion in consolidated depository institution assets may also participate. No institutions that are on the Federal Deposit Insurance Corporation's problem bank list (generally those with a CAMELS rating of 4 or 5), or holding companies of such institutions, are eligible

Institutions with less than \$1 billion in assets on December 31, 2009, are eligible for a capital investment of up to 5 percent of their risk-weighted assets on that date; institutions with more than \$1 billion in assets, but less than \$10 billion, may receive a capital investment of up to 3 percent of risk-weighted assets. The specific form of capital investment has been left to Treasury's discretion. However, House Financial Services Committee Chairman, Barney Frank, has said on the House Floor that the intent is for the Treasury is to have capital investments count as Tier 1 capital. Industry trade groups have already petitioned the federal bank regulators to that effect.

The interest (or dividends) on the capital investment by Treasury will vary depending upon the particular institution's level of small business lending. Initially, the rate will be 5 percent per annum. Within two years of the investment, the rate will be adjusted based on the institution's level of small business lending. The rate will be reduced to 4 percent if the institution has increased its small business lending by 2.5 percent or more, but less than 5 percent, over the baseline established in the legislation. If small business lending has increased by 5 percent to 7.5 percent over the baseline, the rate on the capital investment will be 3 percent. If the increase is 7.5 percent or more, but less than 10 percent, the rate will be 2 percent. If small business lending has increased by 10 percent or more, the rate will be 1 percent. If the institution's small business lending has decreased or remained static, the rate will rise to 7 percent. The rate on the capital investment will increase to 9 percent for all institutions at the end of the four and one-half year period beginning on the date of investment. The legislation generally specifies that a Fund capital investment must be repaid within 10 years of the date of investment.

Institutions interested in participating in the Fund must file an application with their primary federal regulator and, if state-chartered, their state regulator. The application must include a "small business lending plan" that describes how the institution's business strategy and operating goals will allow it to fulfill the borrowing needs of small businesses in its market area, as well as provide "linguistically and culturally appropriate outreach, where appropriate." Treasury and the bank regulator(s) are to consult to determine whether the institution will receive approval for a capital investment from the Fund.

**Treasury will now issue guidelines specifying the form of capital investment, including the term sheet, and application materials to allow eligible institutions to apply for a capital investment from the Fund. The legislation provides that the Fund is not part of the TARP program. However, it specifically requires Treasury to issue guidance to allow eligible institutions to use capital investments from the Fund to refinance securities issued to Treasury under the TARP Capital Purchase or Community Development Capital Initiative Programs. For Capital Purchase Program participants that engage in or anticipate significant small business lending, the Fund may represent an attractive opportunity to secure lower rate funding. The legislation is silent on whether TARP conditions, such as executive compensation restrictions, will apply to refinances involving the Fund. Any institution that has missed more than one dividend payment under the Capital Purchase Program is specifically prohibited from refinancing with a Fund capital investment.**

For more information about these issues, please contact the author(s) of this Legal Alert or your existing firm contact.

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