



EXCEL NATIONAL BANK
Excellence in Banking™



November 13, 2008

LETTER OF COMMENT NO. 19

Technical Director – File Reference 1610-100
Financial Accounting Standards Board
401 Merritt 7
PO Box 5116
Norwalk, Connecticut 06856-5116

RE: Proposed FASB Statement, Accounting for Transfers of Financial Assets – An Amendment of FASB Statement No. 140 (File Reference No. 1610)

Dear Technical Director:

Excel National Bank appreciates the opportunity to comment on the Proposed Statement of Financial Accounting Standards, FASB No. 140, *Accounting for Transfers of Financial Assets – An Amendment of FASB Statement No. 140 (No. 1610-100, September 15, 2008)* (the “Proposed Statement”).

We originate Small Business Administration (“SBA”) 7(a) loans. Under the SBA’s 7(a) program, the SBA guarantees a portion (generally 75%) of the loan. A secondary market has developed for the guaranteed portion of SBA 7(a) loans. When the guaranteed portion is participated the originating lender (the “Lender”) enters into a tri-party agreement with the SBA and registered holder or a broker/dealer (“Buyer”). The agreement is documented on the SBA Form 1086 entitled “Secondary Participation Guaranty Agreement.” The SBA Form 1086 specifies a minimum fee of 1% be retained by the Lender. Lenders have sold the guaranteed portion for a premium and retained the unguaranteed portion of the loan and at least the minimum fee of 1% or have sold guaranteed portion of the loan to retain a fee in excess of 1%. After the loan participation the payments received from the borrower are split based on a pro-rata basis, which generally is equal to the percent of the SBA guaranty. However, the Buyer’s interest is reduced by the fee retained by the Lender and other SBA fees. In the event of default the SBA purchases the Buyer’s interest in the loan, and the Lender and SBA share in the liquidation proceeds and expenses on a pro-rata basis. Additionally, if the guaranteed portion was sold for a premium, the lender is subject to two warranties. The first warranty is “If the borrower prepays the loan for any reason with 90 days of the Warranty Date, the Lender must refund any premium received.”¹ The second warranty is “If the borrower fails to make the first three monthly payments due after the Warranty Date and

¹ SBA Form 1086 (6-02), OMB NO.: 3245-0185



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the borrower enters uncured default within 275 calendar days from the Warranty Date. Lender shall refund any premium received.”² The Warranty Date is the date that the loan participation is settled.

Paragraph 8B (a) of the Proposed Statement states, that a participating interest represents a proportionate ownership interest in an entire individual financial asset. How does a SBA guarantee impact the proportionate ownership interest? Also, if the Lender retains a fee greater than the 1% minimum, how does that impact the proportionate interest?

Paragraph 8B (b) of the Proposed Statement states, “All cash flows received from the asset are divided among the participating interests... in proportion to the share of ownership represented by each.” After the guaranteed portion of a SBA 7(a) loan is participated, the Buyer has a full faith and credit guarantee by the United States. Therefore, the Buyer generally receives a market yield on the guaranteed portion that is substantially lower than the borrower’s note rate. Would the difference between the note rate and the Buyer’s guaranteed portion cause the transaction to fail the requirements of paragraph 8B (b) of the proposed Statement?

We agree with several of the earlier comment letters which suggested that origination fees and cash flows received that represent the transferor’s gain or loss on the sale of a portion of a financial asset should be excluded from the requirements of paragraph 8B(b) of the Proposed Statement.

Paragraph 8B(c) of the Proposed Statement states “The rights of each participating interest holder ... have the same priority ...” In the event of a default on a SBA 7(a) loan the SBA purchases the guaranteed portion from the buyer. The lender and the SBA share the proceeds and expenses of the liquidation proportionally. Does the purchase of the guaranteed portion from the buyer result in a failure to meet the requirements of paragraph 8B(c)?

Also, would the 90 day prepayment warranty and the first three monthly payments warranty for SBA 7(a) loans qualify as standard representations and warranties or represent a form of recourse?

We support Robert Traficanti’s, Vice President and Deputy Controller, Citigroup Inc., comment in his letter dated October, 30, 2008 “The concept of a participating interest

² *ibid*



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adds unnecessary complexity to the proposed Statement, which we believe is unwarranted. We recommend that this concept be eliminated from the proposed Statement and, instead, require transfers of both entire financial assets and portions of a financial asset to meet the same criteria for sale accounting... We believe that the application of the requirements in paragraph 9 to all transfers of financial assets, including transfers of a portion of a financial asset, should be conceptually consistent and should not result in two economically identical transactions being accounted for differently.”

We believe that if the participations of SBA 7(a) guaranteed portions fail to meet sales treatment under the new requirements of paragraph 8B of the Proposed Statement, many lenders will abandon the guaranty programs. The result of lenders abandoning the SBA programs will reduce the credit available to small businesses. Providing credit to small businesses is critical to our economy.

Thank you for considering the impact of the Proposed Statement on the SBA 7(a) secondary market.

Sincerely,

William H. McGaughey,
Executive Vice President/Director of Capital Markets
Excel National Bank