



Billing Code 8025-01

SMALL BUSINESS ADMINISTRATION

13 CFR Part 107

RIN 3245-AG67

Small Business Investment Companies: Passive Business Expansion and Technical Clarifications

AGENCY: U.S. Small Business Administration.

ACTION: Final rule; delay of effective date and request for comment.

SUMMARY: On December 28, 2016, the Small Business Administration (SBA) published a final rule to expand permitted investments in passive businesses and provide further clarification with regard to investments in such businesses for the Small Business Investment Company (SBIC) Program, with an effective date of January 27, 2017. On January 26, 2017, SBA published a notification delaying the effective date until March 21, 2017 and re-opened the rule for additional public comment. On March 21, 2017, SBA published another notification to delay the effective date of this rule until May 20, 2017, to give the new administration time to further consider the rule. After reviewing the final rule, SBA is considering removing the provision that would allow SBICs to use a blocker corporation under its regulations if an investor of an SBIC has elected to be taxed as a regulated investment company (RIC) and a direct investment into the operating company would cause the investor to receive or be deemed to receive income that would jeopardize its RIC status. SBA is seeking additional comments regarding the removal of this provision. In order to give the public time to provide comments and for SBA to

review those comments, the effective date of the final rule is delayed until August 18, 2017.

DATES: The effective date of the SBA final rule published December 28, 2016 (81 FR 95419), delayed until March 21, 2017 at 82 FR 8499 and then further delayed until May 20, 2017 at 82 FR 14428, is further delayed until August 18, 2017. Comments on this document must be submitted no later than [INSERT DATE 30 DAYS AFTER THE DATE OF PUBLICATION IN THE FEDERAL REGISTER].

ADDRESSES: You may submit comments, identified by RIN 3245-AG67, by any of the following methods:

Federal eRulemaking Portal: <http://www.regulations.gov>. Follow the instructions for submitting comments.

Mail, Hand Delivery/Courier: Theresa Jamerson, Office of Investment and Innovation, U.S. Small Business Administration, 409 Third Street SW, Washington, DC 20416.

SBA will post comments on <http://www.regulations.gov>. If you wish to submit confidential business information (CBI) as defined in the User Notice at <http://www.regulations.gov>, please submit the information to Theresa Jamerson, Office of Investment and Innovation, 409 Third Street SW, Washington, DC 20416. Highlight the information that you consider to be CBI, and explain why you believe this information should be held confidential. SBA will review the information and make the final determination of whether it will publish the information.

FOR FURTHER INFORMATION CONTACT: Theresa Jamerson, Office of Investment and Innovation, (202) 205-7563 or sbic@sba.gov.

SUPPLEMENTARY INFORMATION: The U.S. Small Business Administration (SBA) Final Rule entitled Small Business Investment Companies: Passive Business Expansion and Technical Clarifications, 81 FR 95419 (December 28, 2016), had an effective date of January 27, 2017. The Final Rule would expand permitted investments in passive businesses, provide further clarification with regard to investments in such businesses, and add certain requirements to improve SBA's ability to monitor such investments. The Final Rule would also make a conforming change to the regulations regarding the amount of leverage available to SBICs under common control to be consistent with the Consolidated Appropriations Act, 2016, which increased the maximum amount of such leverage from \$225 million to \$350 million.

The January effective date was delayed to March 21, 2017, and the comment period was reopened until February 19, 2017. 82 FR 8499 (January 26, 2017). The March effective date was further delayed to May 20, 2017, for additional review. 82 FR 14428 (March 21, 2017).

After completing its review, SBA is considering removing the provision that would allow SBICs to use a blocker entity under 13 CFR 107.720(b)(3) if an investor in an SBIC, typically a business development company (BDC), has elected to be taxed as a regulated investment company (RIC) and a direct investment into the operating company would cause the investor to receive or be deemed to receive income that would jeopardize its RIC status. This provision was not included in the proposed rule published on October 5, 2016 (78 FR 77377), but was added to the final rule published on December 28, 2016 (81 FR 95419) based on comments SBA received. After further consideration, SBA is concerned that, in light of the increased complexities involved in monitoring and

examining investments structured through blocker entities using this provision may increase risk to the SBIC program unless SBA were to increase examination resources to monitor these complex transactions. SBA notes that the final rule provides, among other things, two other exceptions to the passive business regulation -- the blocker corporation exception for SBICs with tax exempt investors to avoid unrelated business taxable income (UBTI) and a similar exception for SBICs with foreign investors to avoid effectively connected income (ECI). SBA continues to believe the number of SBICs that would structure investments through passive entities utilizing these two exceptions is relatively low. Currently, SBA approves approximately five blocker corporation exceptions for UBTI each year and SBA expects that, after the rule is effective, only a few SBICs will use the ECI exception. On the other hand, there are currently 31 SBICs with BDC investors (BDC-SBICs) holding over 23% of SBA's outstanding guaranteed leverage. If the final rule were to become effective in the form published on December 28, 2016, SBA believes that many BDC-SBICs would structure a number of their investments through passive entities. Because BDC-SBICs represent such a large percentage of SBA's portfolio, significant numbers of investments structured through passive entities would pose a monitoring and examination challenge that could expose the program to an unacceptable level of risk unless SBA increased significantly its examination and monitoring resources. Therefore, SBA is considering revising the final rule to remove this provision.

SBA is seeking comments from the public to obtain additional input before making a final decision. To provide SBA with sufficient time to seek additional

comments and make this determination, this notice further delays the effective date by 90 additional days to August 18, 2017.

Dated: April 25, 2017.

A. Joseph Shepard,
Associate Administrator, Office of Investment and Innovation.
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