from SBA at the time their repurchases are completed. In general, when a company repurchases its own stock at a discount (that is, for less than the original issue price), it records an increase in paid-in surplus equal to the discount. Section 301(d) Licensees will follow this general rule, but the increase in surplus attributable to the repurchase must be separately identified (as "Restricted Contributed Capital Surplus") on SBA Form 468 because it is subject to certain restrictions for regulatory purposes.

## V. Contributed Capital and Committed Capital

- i. In general, "contributed capital" refers to funds contributed to a Licensee by private investors (although such funds may also include "qualified nonprivate funds" from State and local government sources, in accordance with the definition of Private Capital in § 107.3). Although some Licensees may obtain financial assistance through the issuance of equity-type securities purchased or guaranteed by SBA, such securities are reported on Form 468 as SBA leverage rather than as contributed capital. The contributed capital of a corporate Licensee consists of the par value of its capital stock (which may consist of one or more classes or stock) and its aggregate paid-in surplus, excluding Restricted Contributed Capital Surplus obtained through the repurchase of 3 percent preferred stock from SBA. For a partnership Licensee, contributed capital consists of proceeds from the sale of partnership interests to the general partners and the limited partners (other than SBA). For all Licensees, contributed capital shall be recorded net of expenses incurred to obtain the capital.
- ii. Capital contributed to a Licensee in the form of non-cash assets requires the prior approval of SBA, unless such assets are physical assets to be currently employed by the Licensee in its operations (see § 107.705). Equity securities issued in exchange for approved non-cash assets will be excluded from a Licensee's Regulatory Capital until the assets received are converted to cash.
- iii. Commitments from Investors. In addition to its contributed capital, a Licensee may have outstanding commitments from individuals or entities to invest additional funds in the Licensee at a future date. Binding commitments from Institutional Investors (as defined in § 107.3) may be included in the Licensee's Regulatory Capital; the principal effects of such inclusion are to increase the Licensee's overline limitation (See § 107.303) and to increase the capital base used in the computation of Capital Impairment (see § 107.210(h)).
- iv. Unfunded commitments from investors shall not be reported as part of the contributed capital of the Licensee on SBA Form 468. The amount of such commitments shall be disclosed in a footnote to the financial statements, which shall separately identify commitments included in Regulatory Capital and any other commitments outstanding. Any significant terms and conditions associated with investor commitments, including the timing of anticipated drawdowns if known, shall also be disclosed.

- W. Unrealized Gain (Loss) on Securities Held
- i. Unrealized Gain (Loss) on Securities Held results from the valuation of Loans and Investments by the Board of Directors or General Partner(s). Unrealized appreciation is recognized for valuations above cost and unrealized depreciation is recognized for valuations below cost. Unrealized gain or loss is the aggregate amount obtained by summing the unrealized appreciation or depreciation of all Loans and Investments, net of any estimated future income tax effects.
- ii. Unlike some other types of investment companies, such as mutual funds, SBICs do not report changes in net unrealized appreciation or depreciation in the Statement of Operations. Instead, such changes are recorded directly in the capital account, Unrealized Gain (Loss) on Securities Held. SBA requires this treatment for two reasons: (1) because most securities held by SBICs have no readily ascertainable market values and valuation of such securities is highly subjective, SBA prefers that reported net income not be influenced by changes in valuation; and (2) segregation of unrealized gains and losses on the Statement of Financial Position makes it easier to perform certain computations required by SBA regulations.

## X. Undistributed Realized Earnings

- i. Undistributed Realized Earnings is the defined term used in SBA regulations to represent the earned capital of a Licensee. In general, Undistributed Realized Earnings are the cumulative balance of periodic net investment income (loss) and realized gain (loss) on investments, less dividends or distributions (at times, an SBIC may need to make an adjustment which is not reflected in this general formula). To accommodate regulatory requirements, two components of Undistributed Realized Earnings are presented separately in the financial statements:
- ii. Non-cash Gains/Income consists of (1) gains on the disposition of securities realized in the form of notes, securities or any other non-cash assets; (2) income from investments in pass-through entities (such as limited partnerships) which has not been distributed to the Licensee; (3) dividends received in kind; (4) interest income accrued on deferred interest notes, zero coupon bonds or similar instruments; and (5) delinquent accrued interest converted into a new note or added to the principal of an existing note (the amount of such interest which is included in Undistributed Net Realized Earnings must be reclassified to Non-cash Gains/Income).
- iii. Non-cash Gains/Income represents realized earnings of an SBIC which have been recognized in the Statement of Operations. Such earnings are segregated in the Statement of Financial Position only because they are subject to certain restrictions under SBA regulations, primarily concerning distributions. In effect, Non-cash Gains/ Income can be considered a type of restricted retained earnings.
- iv. Classification of capital gains or other income as non-cash items is intended to be temporary. As a Licensee receives payments on a note, receives distributions from a

- partnership in which it has invested, sells shares of stock received as a dividend or otherwise converts non-cash assets to cash, amounts initially reported as Non-cash Gains/Income shall be transferred to Undistributed Net Realized Earnings.
- v. Undistributed Net Realized Earnings is a residual, computed by subtracting the balance in Non-cash Gains/Income from Undistributed Realized Earnings. If an SBIC holds treasury stock, Undistributed Net Realized Earnings are restricted (i.e., not available for distribution) to the extent of the cost of such treasury stock.

## Y. Retained Earnings Available for Distribution

- i. Retained Earnings Available for Distribution represents, in most cases, the maximum amount that an SBIC may distribute to investors. For SBICs which have received financial assistance from SBA in a form other than debentures, the term "investors" encompasses SBA as well as private investors.
- ii. In some instances, SBA is entitled to receive payments from Retained Earnings Available for Distribution on a priority basis, and must receive these payments before any amounts may be distributed to investors or transferred to private capital. Dividends (or equivalent distributions) on 4% preferred securities issued by Section 301(d) Licensees are examples of such payments. In other cases, SBA may be entitled to receive payments from Retained Earnings Available for Distribution in proportion to any distributions received by private investors. Profit participations on Participating Securities are an example of this type of payment.
- iii. For most Licensees, Retained Earnings Available for Distribution is computed by subtracting unrealized depreciation on Loans and Investments from Undistributed Net Realized Earnings (excluding any restricted amounts). Unrealized depreciation and unrealized appreciation are not netted in this computation.
- iv. For Section 301(d) Licensees which have issued 4% preferred securities, there is one additional element in the computation. Because 4% distributions in arrears are accrued and charged against Undistributed Net Realized Earnings, they must be added back to determine Retained Earnings Available for Distribution.
- v. Although partnerships do not ordinarily report retained earnings as such, partnership SBICs must compute Retained Earnings Available for Distribution in the same manner as corporate SBICs. Further discussion of the equity classifications used by partnership SBICs in financial reporting to SBA appears in paragraph Z ("Partnership Capital Accounts") of this section V.
- vi. If a Licensee has negative Retained Earnings Available for Distribution as of the end of a fiscal period, and has made or declared a distribution during such period, the distribution may have violated SBA regulations. It is the Licensee's responsibility to show, to the satisfaction of SBA, that it had sufficient Retained Earnings Available for Distribution at the time the distribution was made. In particular, a Licensee should