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On behalf of its agency, U.S. Small Business Administration

UNITED STATES DISTRICT COURT
NORTHERN DISTRICT OF CALIFORNIA
SAN JOSE DIVISION

SECURITIES AND EXCHANGE
COMMISSION

Plaintiff,

v.

SMALL BUSINESS CAPITAL CORP.;
MARK FEATHERS; INVESTORS PRIME
FUND, LLC; and SBC PORTFOLIO FUND,
LLC

Defendants.

) Case No. CV12-03237
)
) **OPPOSITION OF U.S.**
) **SMALL BUSINESS**
) **ADMINISTRATION TO**
) **RECEIVER'S MOTION**
) **FOR APPROVAL OF**
) **DISTRIBUTION PLAN AND**
) **AUTHORIZATION TO MAKE**
) **INTERIM DISTRIBUTIONS**
)
)
) Ctrm: 4 - 5th Floor
) Judge: Hon. Edward J. Davila

I. INTRODUCTION

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2 Claimant U.S. Small Business Administration (“SBA”), an Agency of the U.S.
3 Government, respectfully submits this opposition to the Receiver’s Motion for Approval
4 of Distribution Plan and Authorization to Make Interim Distributions (the “Motion”).
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6 The Receiver’s Motion proposes to pool the assets of the Receivership Entities (as
7 defined in the Motion) and distribute all but approximately \$1.6 million of the
8 approximately \$20 million in cash in the estate as an interim distribution to the investors
9 in the Receivership Entities. SBA has timely filed a claim for approximately \$24
10 million against the Receivership Entities. None of the approximately \$19 million in cash
11 to be distributed by the Receiver will be paid to SBA on account of its claim nor does the
12 Receiver propose to set aside any funds in reserve for SBA’s claim. SBA opposes the
13 proposed interim distribution plan upon the grounds that it violates the Federal Priority
14 Statute, 31 U.S.C. § 3713, which provides that the Receiver must pay debts owing to the
15 United States first before paying other creditors or investors. At a minimum, the
16 proposed interim distribution plan must include the full payment of SBA’s liquidated
17 claim and provide SBA with some assurance that there will be adequate funds available
18 to resolve SBA’s contingent claim.
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22 **II. SBA’S OPPOSITION TO RECEIVER’S PROPOSED INTERIM**
23 **DISTRIBUTION PLAN**

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25 The Receivership Entities were engaged primarily in the business of small business
26 lending through two SBA loan programs. One of the Receivership Entities, Small
27 Business Capital, LLC, holds a license from SBA to operate as a Small Business Lending
28 Company (“SBLC”).

1 SBLCs are private non-depository institutions that are licensed and regulated by SBA.
2 See, 13 C.F.R. § 120.470. SBLCs participate in and make loans under SBA's 7(a) Loan
3 Program. The majority of the 7(a) loans made by Small Business Capital, LLC were sold
4 to investors in SBA's 7(a) secondary market. See, 13 C.F.R. § 120.600 *et seq.* SBA has
5 unconditionally guaranteed the timely payment of those loans to the investors based upon
6 the full faith and credit of the United States. Small Business Capital, LLC has 44 SBA
7 7(a) loans on its books with a total SBA guaranty exposure of approximately \$32 million.

9 Three other Receivership Entities, Investors Prime Fund, LLC, SBC Portfolio Fund,
10 LLC and SBC Senior Commercial Mortgage Fund, LLC, originated small business loans
11 through a separate SBA loan program. Certain of those loans were sold by the three
12 Receivership Entities to investors in SBA's 504 secondary market under a temporary
13 program (the "FMLP Program") authorized by Section 503 of the American Recovery
14 and Reinvestment Act of 2009. See, 13 C.F.R. § 120.1700 *et seq.* SBA has
15 unconditionally guaranteed the timely payment of pools of the 504 FMLP Program loans
16 to investors in SBA's 504 secondary market also based upon the full faith and credit of
17 the United States. The three Receivership Entities have 12 SBA 504 FMLP Program
18 loans on their books with a total SBA guaranty exposure of approximately \$26 million.

21 In March 2013, SBA conducted a targeted review of the Receivership Entities' 7(a)
22 and 504 FMLP Program loan portfolios. Based on SBA's findings from the targeted
23 review, SBA timely filed a contingent claim in the amount of \$24,147,396.40 against the
24 receivership estate. SBA also filed a liquidated claim in the amount of \$34,269.00
25 against the receivership estate for fees incurred by SBA in connection with the targeted
26 review. SBA's contingent claim, as noted, is based upon evidence of loan irregularities
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1 that SBA discovered in the Receivership Entities' SBA 7(a) and SBA 504 FMLP loan
2 portfolios in the amounts of \$2,711,712 and \$21,435,684.40, respectively.

3 The basis for SBA's claim is related to certain regulatory and contractual obligations
4 the Receivership Entities owe to SBA with respect to the origination, sale to the
5 secondary markets, closing, servicing and/or liquidation of the SBA 7(a) and SBA 504
6 FMLP Program loans that are currently controlled and serviced by the Receivership
7 Entities. SBA's claim was filed in accordance with the claim procedures that were
8 approved by this Court and provides sufficient documentation and citations in support of
9 the claim. Although the Receiver has objected to SBA's claim, he has provided no legal
10 or factual basis for his objection. SBA has filed an opposition to the Receiver's objection
11 to SBA's claim and has requested that the Court set a briefing schedule on the objection.
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14 In the Motion, the Receiver states that he is negotiating with the SBA concerning the
15 SBA's claim and the sale of the Receivership Entities' SBLC license and SBA loan
16 portfolios. The Receiver notes that at this time no reserve has been set for SBA's claim
17 because the Receiver believes that SBA's claim is tied to the existing loan portfolio.
18 SBA agrees that any sale of the 7(a) loans and the 504 FMLP Program loans will be
19 subject to SBA's claim pursuant to the provisions of 13 C.F.R. § 120.432 and 13 C.F.R. §
20 120.1707, respectively. However, it is premature to distribute essentially all of the cash
21 of the receivership estate before the Receiver has made any attempt to sell the SBA loan
22 portfolio to qualified buyers in accordance with SBA's Loan Program Requirements.
23 SBA encourages the Receiver to immediately seek qualified buyers for the 504 FMLP
24 Program loans and to continue to work with SBA to develop procedures for the sale of
25 the 7(a) loan portfolio and the SBLC license.
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1 SBA opposes the Receiver's proposed interim distribution plan. Pursuant to the
2 Federal Priority Statute, 31 U.S.C. § 3713(a), the Receiver must pay debts to the United
3 States first before paying any other creditor or investor, with the exception of
4 administrative expense creditors. The Federal Priority Statute is to be "liberally
5 construed so as to effect the public purpose of securing debts owed to the United States."
6 United States v. Whitney, 654 F.2d 607, 609 (9th Cir. 1981) (*citing* Bramwell v. United
7 States Fidelity & Guaranty Co., 269 U.S. 483 (1926)). A court-appointed receiver who
8 knowingly distributes an insolvent debtor's assets in disregard of the United States' claim
9 may be held personally liable under the Federal Priority Statute. See, 31 U.S.C. §
10 3713(b). See also, United States v. Crocker, 313 F.2d 946, 948-49 (9th Cir. 1963).

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13 The Receiver's proposed interim distribution plan intentionally seeks to exclude SBA
14 from receiving any distribution and provides no assurance that there will be any funds
15 available to resolve SBA's claim. Until a resolution can be reached with respect to
16 SBA's claim, the Receiver should not be permitted to make the proposed interim

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1 distribution. At a minimum, the Receiver should be required to reserve more than the
2 \$1.6 million he has offered to set aside for future administrative expenses.

3 Respectfully submitted,
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9 Date: November 26, 2013

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