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Commercial Lending: Venture Loans to Companies in an Early, Expansion, or Late Stage of Corporate Development

Replaced - See OCC 2025-45

To

Chief Executive Officers of All National Banks, Federal Savings Associations, and Federal Branches and Agencies; Department and Division Heads; All Examining Personnel; and Other Interested Parties

As of March 20, 2025, the OCC will no longer examine for reputation risk. Refer to OCC Bulletin 2025-4.

Summary

The Office of the Comptroller of the Currency (OCC) is issuing this bulletin to inform banks[1] about policy guidance that applies to commercial loans to early-, expansion-, and late-stage companies. This bulletin refers to these loans as "venture loans." There is heightened uncertainty and higher probability of failure associated with new business ventures. The OCC expects banks engaging in venture lending to do so in a safe and sound manner, in compliance with applicable laws and regulations, and with support from sound risk management systems. Before making any loan,

bank management should identify the purpose of the loan and the source of repayment. In addition, bank management should assess the ability of the borrower to repay the loan in a timely manner. Documentation maintained by the bank should support the decision to grant the credit and allow for follow-up monitoring, as the bank would perform with any loan. OCC examiners will scrutinize loan commitments that are underwritten without an adequate assessment of the borrower's capacity to repay and will determine whether such loans should be subject to supervisory criticism. Examiners will ask banks to determine the impact that any weak venture loan underwriting standards may have on the assumptions used in calculating loan loss reserves.

Note for Community Banks

This bulletin applies to all OCC-regulated banks, including community banks, that engage in or are considering engaging in venture lending.

Highlights

This bulletin

- presents background information on venture lending.
- describes venture lending risks.
- discusses risk management practices for venture lending.
- provides guidance for risk-rating venture loans and evaluating repayment capacity.

Background

The OCC encourages banks to engage in lending activities that are creditworthy and consistent with safe and sound banking principles, including lending to small and medium-sized businesses and minority-owned businesses.[2] The OCC has observed that some banks have added or are considering adding new commercial lending activities targeting high-risk borrowers in an early-, expansion-, or late-stage of corporate development.[3] The OCC refers to these activities as "venture lending" and borrowers as "venture borrowers" or "venture-backed companies."

The OCC generally does **not** characterize the following forms of credit as "venture loans": (i) loans to businesses that primarily rely on their own internally generated cash flow, rather than equity infusions, to maintain and grow operations; (ii) loans made under lending support programs when federal, state, or local government guarantees sufficiently mitigate credit risk (e.g., U.S. Small Business Administration guarantees);[4] and (iii) loans made under special purpose credit programs (SPCP) as described in 12 CFR 202.8.[5] Additionally, qualified banks may eliminate unnecessary documentation for certain loans as described in the "Interagency Policy Statement on Documentation for Loans to Small- and Medium-sized Businesses and Farms" conveyed by Banking Bulletin 1993-18.

Venture lending supports new business formation and can improve access to capital for growth companies. However, new business ventures have a high probability of failure. Venture borrowers typically have not reached a mature stage of corporate development and may not exhibit sustainable positive cash flows or collateral to support loan repayment. Thus, venture lending often involves banks accepting high-risk characteristics that banks normally avoid when originating conventional commercial loans to borrowers with reliable cash flows and positive earnings.[6] Therefore, venture borrowers warrant strong underwriting analysis and monitoring commensurate with the level of risk in such loans. Venture lending facilities should include appropriate credit enhancements to mitigate the elevated risk of borrower failure.

This bulletin divides the broader category of venture borrowers into two segments: (i) early-stage and expansion-stage companies and (ii) late-stage companies. Borrowers in both segments may not have sustainable cash flows to service debt or sufficient assets to use as collateral support for a conventional commercial loan. The ability to service debt means the borrower will be able to pay all interest, fees, and principal on all debt obligations in accordance with original contractual terms.

Early- and Expansion-Stage Companies

Early-stage companies are in the initial stages of business concept and planning. These emerging companies have limited or no revenues and often have high expenses. As a company moves from an early stage of development to an expansion stage of development, it increases hiring, focuses on product or service development, and invests in demand generation and market introduction.

Subsequent equity financing raised from external investors is frequently cited by lenders as the source of repayment for loans to early- and expansion-stage companies. Industry participants sometimes refer to companies that rely on subsequent external equity financing for continuing operations as “investor-dependent” companies, in contrast to companies that primarily rely on their own internally generated cash flow, owner-infused equity, or seed capital to maintain and grow operations.

Early- and expansion-stage borrowers have limited operating histories for lenders to evaluate and underwrite. Instead, lenders often consider the quality of these borrowers’ investors or sponsors, the certainty of subsequent capital raises by the borrower, the borrower’s recent post-money valuation,[7] and the borrower’s projected cash burn relative to cash on hand. Reliance on these factors without appropriate credit enhancements—for example, through controlled cash collateral or other measures—may result in excessive risk taking by lenders.

Late-Stage Companies

Companies in the late stages of the development cycle also face uncertainty and often are characterized by significant rollout of new products or services to the market, accompanied by the potential for accelerating sales growth. Borrowers in this stage of corporate development may be ramping up or may have already reached significant scale. But late-stage companies continue to warrant strong underwriting analysis and monitoring because cash flow may be negative, intermittent, or insufficient to service debt, resulting in dependence on secondary sources of repayment. Secondary sources of repayment for late-stage companies can vary and may include private equity financing, public debt or equity, the sale of assets, or liquidity from earlier fundraising.

Venture Lending Risks

Primary risks in venture lending can include unproven cash flows, untested business models, difficulty projecting future cash flows, high liquidity needs, high investment spend, and limited refinancing or business takeout/exit options. Borrowers in an earlier stage of development (i.e., the early or expansion stages) are typically riskier than those in a later stage of development. Later-stage companies may be more likely to generate sustainable cash flow despite significant expenses related to company expansion. With these characteristics in mind, it is important for lenders to clearly differentiate between (i) venture loans for which future repayment depends on a borrower's investments in new products, new markets, higher than historical growth, liquidity coverage of cash burn, or subsequent fundraising from equity investors and (ii) conventional loans to mature companies with structures based on a borrower's existing sound operating model, internally generated cash flow, and the life of its assets.

Considering this background, venture borrowers are companies that, when compared with mature companies, may

- have a shorter business history.
- exhibit a higher risk of business failure because they prioritize growth over profitability.
- be pre-product, pre-revenue, pre-positive cash flow, or pre-profit.

Because venture borrowers are not yet mature companies, venture loan facilities sometimes exhibit potential or well-defined weaknesses,[8] including

- incomplete management teams or business infrastructures.
- undeveloped or unproven products or services.
- declining or insufficient liquid assets and working capital.
- negative or insufficient operating cash flow to service or repay debt.[9]
- insufficient assets to pledge as collateral to mitigate high credit risk, or, in the case of cash collateral, an inability or unwillingness to restrict and reserve balance-sheet cash for loan repayment.
- reliance on uncommitted equity funding to provide for the primary source of repayment or to continue operating as a going concern.
- ongoing uncertainty about the borrower's long-term viability.

One or more of these weaknesses may result in deterioration of the repayment prospects for the asset or jeopardize the liquidation of debt, which may warrant prudent credit risk mitigation measures to reduce the risk of loss when a loan defaults. Mitigating factors, however, primarily protect against loss when a loan defaults and generally do not lessen the risk of default. Therefore, mitigating factors' impact on the regulatory risk rating should be negligible until the loan is classified. Risk ratings should not overstate how much of a loan's credit risk is mitigated.

Venture loans without satisfactory repayment sources or structural protections should be risk-rated and reserved for appropriately and given appropriate accrual treatment. A special mention or classified regulatory risk rating remains appropriate whenever potential or well-defined weaknesses are present. For some substandard assets, the likelihood of full collection of interest and principal may be in doubt; such assets should be placed on nonaccrual.

Risk Management

Given the inherent risks associated with venture lending, the OCC expects banks undertaking venture lending to establish appropriate operational and managerial standards consistent with the safe and sound practices articulated in the "Interagency Guidelines Establishing Standards for Safety and Soundness" (the Guidelines).[10] The Guidelines provide that banks should establish and maintain loan documentation practices that enable the bank to make an informed lending decision, assess risk, and assess the borrower's ability to repay the indebtedness in a timely manner. The Guidelines also provide that banks should establish and maintain prudent credit underwriting practices. This includes, before credit commitment, considering the borrower's overall financial condition and resources.

The Guidelines describe requirements for controls to safeguard and manage assets and the need for loan documentation practices that provide for appropriate administration and monitoring of loans. Control functions providing independent and objective assessment, reporting, and assurance can help banks identify, measure, monitor, and control risk and reduce the risk of loss.

Examples of appropriate general operational and managerial practices for venture lending include

- business or lending plans or strategies appropriate for the bank's size and complexity, including a clear risk appetite statement and risk limits for venture lending approved by the board of directors.
- qualified staff with relevant experience lending to startup or high-growth companies.[11]
- internal reporting and management information systems to help identify, measure, monitor, and control venture lending risks. Sometimes venture lending is isolated to a specific portfolio, but often it is found in other lending segments (e.g., technology, health care, and leveraged lending) throughout a bank's loan portfolio. It is important for banks to have the ability to aggregate venture exposures from across the bank's business lines.
- tracking and ongoing monitoring of any special mention or classified loan originations and exceptions to internal bank policies.[12]

- systems to identify problem assets and take corrective actions to prevent deterioration in those assets.
- stress testing to identify deterioration in the venture portfolio or aggregated venture lending exposure to help ensure that the bank maintains capital and liquidity to withstand adverse conditions.
- timely and accurate risk-rating processes and appropriate credit risk review processes to identify problem assets.[13]
- maintenance of an appropriate allowance for credit losses.

Concentrations of venture lending also warrant the following enterprise-wide risk management practices:

- satisfactory liquidity risk management, including evaluating the level of diversification of a bank's current and prospective funding sources, both on and off the balance sheet; the degree of reliance on short-term, volatile sources of funds, including short-term deposits, borrowings, and brokered deposits, to fund longer-term assets; and the trend and stability of deposits.[14]
- a capital planning process that identifies and evaluates all material risks of venture lending, the amount of capital appropriate for material risks, and a strategy to maintain adequate capital.[15]

Examples of appropriate lending practices for venture lending include

- well-defined policies, procedures, and underwriting standards for venture lending.
- approving only those loan requests that (i) meet the bank's stringent underwriting standards, (ii) have sustainable repayment sources, and (iii) are consistent with appropriate concentration limits for this type of lending.
- loan monitoring that includes obtaining the borrower's financial projections, developing base case and downside projection scenarios, and then monitoring

performance against plan, any cash burn and remaining months liquidity (RML), and the borrower's ability to operate as a going concern.[16]

- mechanisms to risk-rate assets, prevent deterioration in those assets, and take corrective actions to resolve problem assets in a timely manner.
- frequent and robust borrower financial reporting requirements consistent with risk (for example, annual audited financial statements, periodic borrower-prepared financial statements, borrower-prepared interim cash reporting, and borrower-updated projections).
- loan structures with appropriate tenor, repayment capacity, collateral, and covenants.
- loan structures that include frameworks for effectively controlling risk (e.g., protecting collateral) including, for example, the ability to sweep cash to reduce outstanding debt upon an event of default.

The degree to which a borrower's business model is unproven and the degree to which reaching scale is required for a borrower's profitability should influence the number and nature of structural protections or credit enhancements, including the amount of cushion expected from liquidity and projected debt service coverage. Strong lending practices, including structural protections and credit enhancements, increase in consequence the earlier a borrower is in its stage of development or the further away the borrower is from generating positive free cash flow sufficient to repay debt.

Risk Appetite and Risk Limits

A bank's board of directors and senior management establish and communicate the bank's risk appetite through policies and procedures that define responsibility and authority.[17] A bank's venture lending practices should be consistent with the bank's risk appetite, promote an appropriate balance between risk taking and growth, and be consistent with established venture lending policies and procedures.

The board and senior management are responsible for setting the bank's risk limits.[18] It is important for banks to monitor growing or material exposures in venture loans. Consistent with safety and soundness standards,[19] a bank should establish and maintain prudent credit underwriting practices that take adequate account of concentration of credit risk. A bank should also consider the size and potential risks of material asset concentrations when establishing and maintaining systems to identify and prevent problem assets.[20] Additionally, the bank's allowance for credit losses will normally consider the existence, growth, and effect of any concentrations of credit.[21] The inherent risks associated with venture lending can intensify concentration risk. This bulletin does not intend to normalize or encourage concentrations in venture lending.

Venture lending can occur across industries or borrower stages of development but can still create a pool of exposure to borrowers that (i) share common risk characteristics attributed to companies that are not yet mature (e.g., pre-product, pre-revenue, pre-positive cash flow, pre-profit, inadequate positive cash flow to service debt, insufficient collateral, and stage of development) and (ii) depend on balance-sheet cash, commonly on deposit with their lenders, to cover operating losses or net losses associated with borrowers in the early, expansion, and later stages of development. Some banks may establish overall limits and sublimit for material groups of segmented exposures. Material growth or overall exposure in venture lending may lead to higher expectations regarding risk management (e.g., stress testing and management information systems) and greater amounts of regulatory attention.[22]

The OCC has not set risk limits or established a bright line limiting a bank's volume of venture lending. It remains the responsibility of the bank's board and management to demonstrate to examiners that the bank's activities are consistent with the bank's risk appetite, maintained within established risk limits, appropriately documented and underwritten, accurately risk-rated, and sufficiently reserved.[23] A bank's volume of venture lending should be appropriate to the bank's size and complexity and should not pose a challenge to management or present unusual or significant risk to the bank.

Risk-Based Capital Treatment

In general, banks are required to assign a 100 percent risk weight to all corporate exposures that are not 90 days or more past due or on nonaccrual status,[24] including venture loans, for risk-based capital purposes if the credit risk of the exposure is not mitigated through a financially capable guarantor, eligible guarantee, or qualifying financial collateral.

Notwithstanding the minimum requirements, the OCC expects banks to maintain capital commensurate with the level and nature of all risks to which the bank is exposed. The OCC also expects bank management to identify, measure, monitor, and implement adequate controls over the bank's risks.[25]

Risk-Rating Venture Loans and Evaluating Repayment Sources

Venture loans originated with a non-pass risk rating are inconsistent with safe and sound lending standards. Banks' venture lending standards should deter the origination of loans rated non-pass at inception, unless the origination is part of a risk mitigation strategy in which the origination intends to improve an existing non-pass loan.

When evaluating and risk-rating venture loans, banks should

- avoid weakening underwriting standards to accommodate venture loan originations.[26]
- evaluate and risk-rate venture loans similarly to other commercial and industrial loans based on existing supervisory and policy standards. This includes existing guidance and longstanding regulations such as those

regulations establishing operational and managerial standards relating to loan documentation, underwriting, and asset quality.[27]

- focus credit analysis on repayment capacity. The OCC expects banks to rate credit risk based on the borrower's expected performance (i.e., the likelihood that the borrower will be able to service its obligations in accordance with the terms).[28] When evaluating expected performance, it is appropriate to focus on a borrower's
    - historical performance against plan.
    - reliability of projections. OCC examiners will scrutinize projections exhibiting
        - prolonged periods to reach positive free cash flow.
        - positive cash flows that are heavily weighted in later years of the projection period.
        - revenue and expense assumptions that are not properly supported by lender analyses of factors including the borrower's stage of development, competitive differentiation, addressable market, projected market share, time to market, and rate of adoption.
    - ability to generate cash flow sufficient to repay debt and de-lever.
    - ability to rely on cash liquidity explicitly reserved for debt repayment, if any.
    - committed equity financing, if any, that could provide for repayment. OCC examiners will consider whether committed equity financing is contingent on the borrower meeting certain performance milestones and whether the borrower is likely to successfully meet those milestones.
- consider the risk profiles of venture borrowers and determine, based on the borrower's expected financial performance and long-term viability, whether there are sustainable primary and secondary sources of repayment. To be consistent with the operational and managerial standards described in the Guidelines, venture loans should include sustainable repayment sources.

- consider the potential effects of inconstant market conditions on the borrower's ability to execute its business plan, raise additional private or public capital, maintain its equity valuation, or exit via merger or acquisition.

Consistent with the OCC's treatment of other commercial loans, regulatory ratings of pass for venture loans are the exception rather than the rule when sustainable primary and secondary repayment sources are absent.[29] Venture loans that lack a satisfactory primary source of repayment, such as reliable operating cash flows, are normally not rated pass. The primary consideration in a credit risk assessment is the strength of the primary source of repayment. Examples of sustainable primary sources of repayment include (i) sufficient current and expected business cash flow to cover fixed charges and repay debt and (ii) controlled collateral support. When there are well-defined weaknesses, or if the primary repayment source weakens and default probability increases, collateral and other protective structural elements have a greater bearing on the rating. As a general principle, examiners should not classify or rate as special mention the portion of assets covered by a Federal Deposit Insurance Corporation loss-sharing agreement.

The following examples are intended to help banks when evaluating repayment capacity.

> ***An uncommitted future equity raise is not a satisfactory primary source of repayment.***

Venture lenders sometimes cite the potential for subsequent equity funding as the primary source of repayment for venture loans.[30] Uncommitted externally generated equity funding is not a sufficient source of repayment and is not a sustainable source of cash. Banks should generally avoid loans that are underwritten from this equity perspective rather than from a credit perspective.

The OCC acknowledges that new funding from new or existing investors may be one avenue for loan repayment. Venture investors, however, normally prefer to see their capital earmarked for new growth and value creation rather than repaying debt related to old growth. The OCC also recognizes that venture capital investors have a long history of helping their portfolio companies navigate challenges and succeed. Absent a contractual guarantee to the bank, however, venture investors' fiduciary duty is to their limited partners. This fiduciary duty is superior to any perceived duty to honor what some lenders refer to as an "implied guarantee" to continue to support a portfolio company or repay that portfolio company's debt to protect the venture investor's reputation with the bank.[31] There normally needs to be economic incentive in alignment with fiduciary duty before a venture investor provides new or additional funding. Therefore, new capital is only deemed a reliable repayment source when there is documentation of a legally binding commitment from reputable investors or lenders with the willingness and capacity to fund and the intent to use those funds to repay existing debt.

When relying on committed new funding, banks should verify that investors, as individuals or through specified financing vehicles or funds, have the financial wherewithal (also known as "dry powder") and the legal right to honor their commitments. Legal enforceability is an essential requirement for new equity capital, follow-on equity funding, or potential replacement debt from a new lender to be considered sufficient to mitigate risk of loss when other sources of repayment are insufficient. Banks should also consider whether committed equity funding is contingent on the borrower meeting certain performance milestones and whether the borrower is likely to meet those milestones.

> ***A venture borrower's unrestricted and declining cash balance is normally not a sustainable primary source of repayment.***

In lieu of sustainable positive operating cash flow generation, venture borrowers typically have ample amounts of initial unrestricted cash or cash equivalents on their balance sheets, having raised capital from angel investors,[32] venture capital funds, or other investors.

Abundant initial balance-sheet cash can be credit positive. Banks should continue to evaluate a borrower's sources of liquidity in conjunction with all relevant aspects of credit risk when determining a loan's risk rating. This includes analyzing a borrower's cash needs, cash burn rate, loan maturity date, and structural controls to determine whether available liquidity offers sufficient mitigation to a compromised primary source of repayment.

Some venture lenders have advocated that underlying collateral secured by a first priority blanket lien—for example, unrestricted cash on the balance sheet—provides a reliable primary source of repayment. An unrestricted and declining cash balance, however, provides a tenuous source of repayment for venture loans unless there are strong controls in place to ensure that the borrower will maintain sufficient liquidity to mitigate potential or well-defined weaknesses.

If the expected case is that a venture borrower's liquidity will be unrestricted and will be consumed to fund projected negative operating cash flow rather than repay debt and there will be insufficient projected remaining cash to repay the debt commitment at loan maturity, then the liquidity does not qualify as a sustainable source of cash that meets the definition of a satisfactory primary repayment source. Alternatively, if reasonable projections demonstrate that a borrower's unrestricted cash liquidity is expected to cover all projected cash burn without reliance on the loan facility and with ending liquidity remaining sufficient to repay the commitment in its entirety at maturity, then the liquidity may be considered as one factor that may partially compensate for a compromised primary source of repayment.

Nevertheless, absent controls and specific pledges ensuring that liquid collateral remains available at all times to repay the debt, the OCC continues to view liquidity as a secondary repayment source for venture loans (refer to the exception in the "Asset-based lending receives an exclusion" section of this bulletin). Despite this secondary support, the rating assessment, until a default has occurred or is highly probable, is generally based on the expected strength of the primary repayment source.[33]

Controlled cash that is reserved and pledged to cover the debt commitment is considered a sustainable source of cash. Pledging or restricting balance-sheet cash would provide collateral control, but doing so may negate the venture borrower's reasons for having cash balances because liquidity on a venture borrower's balance sheet is usually unrestricted and available for growth expenditures rather than debt repayment. Therefore, venture borrower initial cash positions are usually expected to decline because of negative operating cash flow resulting from expenses associated with the venture's growth (i.e., projected cash burn).[34]

To attempt to address risks from declining cash balances, lenders often establish a covenant related to RML, which can be calculated as the result of dividing the borrower's unrestricted cash at a given moment in time by the borrower's average monthly cash burn for a prior period, such as three months. An RML covenant provides the lender a limited amount of control and enables the lender to measure the amount of time until a cash-burning borrower runs out of cash and must raise additional capital. This is known as measuring the borrower's "runway" and enables the lender to engage with the borrower or its sponsor to understand the likelihood of additional equity funding occurring and to potentially encourage refinancing or loan workout.

Notably, the RML covenant is not necessarily set at a level that provides for full repayment of the loan, and a covenant requiring the borrower to maintain cash on hand in an amount sufficient to repay the entire loan is not normally included in the loan agreement. A loan structured with an RML covenant and a short loan tenor may still exhibit significant credit risk and potential or well-defined weaknesses when otherwise abundant liquidity is unrestricted.

Recurring revenue is not equivalent to sustainable repayment capacity.

Certain venture lenders specialize in making recurring revenue lines of credit to borrowers that have high volumes of contracted or subscription revenues but limited or negative cash flow (e.g., recurring revenue loans made to software-as-a-service companies and other businesses with recurring revenues and low customer churn). Frequently, a high percentage of these borrowers' customers renew their contracts because of inertia or to avoid high switching costs. A borrower may have abundant recurring revenue. Recurring revenue is not, however, equivalent to sustainable repayment capacity.

Even with recurring revenue, it can be challenging for companies that are not yet mature to exhibit sufficient cash flow, collateral, or net worth to repay debt.[35] While recurring revenue is credit positive, as is customer retention, banks should continue to consider all other relevant factors when determining whether there are satisfactory repayment sources in recurring revenue loans to venture borrowers.

Banks sometimes rely on “harvest scenarios” as one method of estimating operating cash flows in recurring revenue lines of credit. The harvest approach eliminates what are deemed as “nonessential” expenses from cash flow projections, resulting in cash flows that would be achieved from remaining pre-existing contracted revenues in an orderly wind-down scenario when going-concern expenses are absent. Thus, the cash flows in a harvest scenario can be substantially higher than would be expected from a traditional going-concern analysis.

Examiners will scrutinize the harvest approach because it can result in calculations that result in lower leverage ratios and faster repayment periods as compared with a base-case going-concern scenario. The most realistic financial projections should be used when measuring a borrower’s capacity to repay and de-lever. Therefore, risk-rating of recurring revenue lines of credit should normally begin with base-case cash flow projections inclusive of all planned expenses and capital expenditures representing the expected borrower financial performance using assumptions that are deemed most likely to occur.

When there are well-defined weaknesses in the primary source of repayment such as the expected base-case operating cash flow, alternative scenarios such as curtailing discretionary growth investments have a greater bearing on the risk rating. Notwithstanding the use of alternative scenarios, the rating assessment, until default has occurred or is highly probable, should be based on the expected strength of the primary source of repayment in consideration of the borrower’s expected performance. Analysis that considers whether the borrower would be left with a viable business if the borrower were to curtail discretionary expenses or growth investments should not unduly influence the rating assessment until the loan is special mention or classified.

Asset-based lending receives an exclusion.

Fully monitored and controlled asset-based loans (ABL) to early-, expansion-, and late-stage companies are a distinct product excluded from this guidance. ABLs enable reliance on collateral that is subject to the bank's control, liquid, properly margined, efficiently valued by credible independent sources, and within the bank's ability to monitor and prevent deterioration in the underlying collateral. Consistent with existing supervisory practices, the OCC does not discourage standalone, well-structured ABLs with strong lender monitoring and controls and expects banks to continue to engage in the sound risk management associated with traditional asset-based lending. The ABL exclusion is not applicable whenever a facility lacks evidence of the full monitoring and controls typically associated with ABL.[36]

Further Information

Please contact Barry A. Mills, Director for Commercial Credit Risk Policy, at (202) 649-6770, or contact your supervisory office.

Grovetta N. Gardineer
Senior Deputy Comptroller for Bank Supervision Policy

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[1] "Banks" refers collectively to national banks, federal savings associations, covered savings associations, and federal branches and agencies of foreign banking organizations.

[2] For more information on how banks can satisfy the financing needs of minority business entrepreneurs, refer to OCC Advisory Letter 2003-8,"Financing Minority Businesses."

[3] Some banks enter venture lending to develop relationships supported through other profitable banking activities, such as equity capital markets or other investment banking and advisory services. Bank management should remain mindful of the anti-tying provisions of 12 USC 1972, which applies to national banks, and of the anti-tying provisions of 12 USC 1464(q), which applies to federal savings associations. Also refer to OCC Bulletin 1995-20, "Tying Restrictions: Guidance on Tying," and OCC Interpretive Letter No. 982, both of which apply to national banks.

[4] Refer to OCC Bulletin 2021-34, "Small Business Administration Lending: Risk Management Principles."

[5] For more information on SPCPs, refer to OCC Bulletin 2022-3, "Fair Lending: Interagency Statement on Special Purpose Credit Programs Under the Equal Credit Opportunity Act and Regulation B."

[6] Taking credit risk without identifying sustainable repayment sources normally constitutes an unsafe or unsound practice. Refer to 12 CFR 30, appendix A, "Interagency Guidelines Establishing Standards for Safety and Soundness."

[7] A venture-backed company's post-money valuation is its equity value immediately following receipt of its most recent round of equity fundraising. It is appropriate for venture lenders to closely monitor the effects of changing market conditions on access to capital and valuations. Valuation pressures may arise when asset prices are high relative to economic fundamentals. Elevated valuation pressures may increase the possibility of outsize drops in asset prices.

[8] This bulletin neither endorses nor encourages the origination of loans with potential or well-defined weaknesses. These weaknesses can exist irrespective of the borrower's stage of development; they are normally less apparent as the borrower reaches later stages of development or maturity. Weaknesses do not automatically trigger adverse risk ratings. Banks should consider all relevant facts and circumstances when determining risk ratings. For example, when repayment capacity exhibits well-defined weaknesses, analysis shifts to the strength of secondary sources and the potential or expected loss. For more information, refer to the "Risk-Rating Venture Loans and Evaluating Repayment Sources" section of this bulletin.

[9] Venture-backed companies' initial cash positions are often expected to decline. This planned cash burn is intentional and covers anticipated expenses that are necessary for growth.

[10] Refer to 12 CFR 30, appendix A. Also, certain banks are subject to 12 CFR 30, appendix D, "OCC Guidelines Establishing Heightened Standards for Certain Large Insured National Banks, Insured Federal Savings Associations, and Insured Federal Branches."

[11] Venture lending is unique and requires specialized skills drawn from a limited pool of industry talent. Banks are expected to primarily rely on their own talent to engage in this type of lending with qualified bank personnel who have risk management, credit administration, and legal expertise relevant to venture lending.

[12] This bulletin neither endorses nor encourages banks' origination of loans with non-pass risk ratings. Venture loans originated with a non-pass risk rating would be inconsistent with safe and sound lending standards. Banks'

venture lending standards should deter the origination of loans rated non-pass at inception, unless the origination is part of a risk mitigation strategy in which the origination intends to improve an existing non-pass loan.

[13] For more information about credit risk review, refer to OCC Bulletin 2020-50, "Credit Risk: Interagency Guidance on Credit Risk Review Systems."

[14] For more information about liquidity risk management, refer to OCC Bulletin 2010-13, "Liquidity: Final Interagency Policy Statement on Funding and Liquidity Risk Management" and OCC Bulletin 2023-25, "Liquidity: Addendum to the Interagency Policy Statement on Funding and Liquidity Risk Management."

[15] For more information on capital adequacy, refer to the "Capital and Dividends" booklet of the *Comptroller's Handbook.*

[16] For more information, refer to the "Recurring revenue is not equivalent to sustainable repayment capacity" section of this bulletin.

[17] For more information, refer to the "Corporate and Risk Governance" booklet of the *Comptroller's Handbook.*

[18] The OCC applies judgment when determining which quantitative limits should be based on stress testing in banks subject to 12 CFR 30, appendix D.

[19] "Concentration of credit risk is addressed by the safety and soundness standards in 12 CFR 30, appendix A. Specifically, a bank should establish and maintain prudent credit underwriting practices that take adequate account of concentration of credit risk. A bank should also consider the size and potential risks of material asset concentrations when establishing and maintaining systems to identify and prevent problem assets. Refer to 12 CFR 30, appendix A, II.D, "Credit Underwriting," and II.G, "Asset Quality."

[20] Ibid.

[21] For more information, refer to the "Allowances for Credit Losses" booklet of the *Comptroller's Handbook.*

[22] For example, refer to the "Concentrations of Credit" booklet of the *Comptroller's Handbook.*

[23] When evaluating reserves, it is important to consider the unique characteristics of the bank's portfolio and how the bank segments it. For example, a bank might segment its venture loans based on characteristics including borrower dependency on external financial support versus borrower ability to maintain internally generated cash flow from operations sufficient to service all debt. The bank might then further disaggregate those segments into classes that consider such characteristics as borrower stage of development, amount of revenues, and transaction size.

[24] For more information on corporate exposures, refer to 12 CFR 3.32(f). For more information on past due exposures, refer to 12 CFR 3.32(k).

[25] Refer to the "Capital and Dividends" booklet of the *Comptroller's Handbook.*

[26] Refer to appendix F, "Structural Weakness Elements," in the "Rating Credit Risk" booklet of the *Comptroller's Handbook.* For purposes of this bulletin, the term "origination" means a new extension of credit, refinancing, modification of an existing loan agreement, or a renewal of a matured or maturing loan transaction. A refinancing or modification includes any type of restructuring or change to an existing nonmatured loan.

[27] For more information, refer to 12 CFR 30, appendix A.

[28] OCC examiners will evaluate the quality of venture loan terms and conditions. Liberal underwriting may be evident in transactions that lack, for example, sufficient debt service coverage, contractual principal amortization, defined use of loan proceeds, tenors matched to the borrower's risk profile and stage of development, or satisfactory loan covenants.

[29] Refer to the "Rating Credit Risk" booklet of the *Comptroller's Handbook.* Government guarantees are a special case. The portions of loans covered by a U.S. government agency guarantee, if any, are usually accorded a regulatory rating of pass. This may include, for example, loans that are covered by loss-sharing agreements that cap the potential losses that a buyer or lender could incur, with the U.S. government covering anything above that amount.

[30] One market participant's U.S. Securities and Exchange Commission filings publicly described that early-, mid-, or late-stage borrowers "typically have modest or negative cash flows and no established record of profitable operations. Repayment of these loans may be dependent upon receipt by borrowers of additional equity financing from venture capital firms or others, or in some cases, a successful sale to a third party or an IPO" (initial public offering).

[31] If a portfolio company is failing, venture investors normally cooperate with their portfolio company's lenders. This can support orderly wind-down and loan workout activities that can protect against lender losses on venture loans.

[32] Angel investors include high-net-worth individuals or family offices that provide initial startup capital to entrepreneurs forming new ventures.

[33] The "Rating Credit Risk" booklet of the *Comptroller's Handbook* describes this supervisory process.

[34] When evaluating a borrower's free cash flow, there may be scenarios that exclude growth capital expenditures from the free cash flow calculation when those expenditures are pre-funded by balance-sheet cash that is specifically set aside for that purpose. This treatment, however, would not apply to maintenance capital expenditures. Regardless of this treatment, repayment capacity should be evaluated based on sustainable cash flow.

[35] For venture borrowers, net worth or enterprise value are less likely to provide reliable secondary or tertiary sources of repayment because venture borrowers are often asset light, and those borrowers requiring liquidation normally have failed to execute business or growth plans. The business value will suffer when cash flow fails to materialize or cannot be reliably projected.

[36] The "Asset-Based Lending" booklet of the *Comptroller's Handbook* describes the OCC's supervisory process for evaluating ABLs and corresponding risk management practices.

Topic(s): ■ COMMERCIAL CREDIT