5164

DECISION

THE COMPTROLLER GENERAL
OF THE UNITED STATES
WASHINGTON, D. C. 20548

FILE: B-188741 DATE: January 25, 1978

MATTER OF: Bank of Salt Lake, Salt Lake City, Utah - SBA Guaranteed Loan

DIGEST:

1. Small Business Administration (SBA) has authority to purchase guaranteed loan notwithstanding bank's failure to provide SBA with written notification of borrower's default within 90-day period prescribed in applicable regulations, since bank substantially complied with notice requirement by providing SBA with oral notification within prescribed period which contained all information that SBA would have obtained had written notification been furnished.

2. Small Business Administration, through its acceptance and subsequent acknowledgment of receipt of oral notification of borrower's default, as well as by its prior conduct, waived regulatory requirement that notice be in writing. Notwithstanding general rule that officers and agents of Federal Government have no authority to waive or otherwise disregard statutory regulations, some judicial precedent does exist in limited circumstances to allow waiver of regulatory requirement involving matter of procedure such as form notice must take.

This decision is in response to a request from Mr. William C. Turner, Authorized Certifying Officer for the Small Business Administration (SBA), for a ruling by our Office as to SBA's authority to purchase a guaranteed loan made by the Bank of Salt Lake, Salt Lake City, Utah to the Village, Ltd. The certifying officer's hesitancy to certify the Bank's claim for payment arises because of the Bank's failure to notify SBA in writing of the borrower's default within the 90-day period prescribed in the applicable regulations, although oral notification of the default was furnished SBA by telephone.

Based on the information contained in the certifying officer's submission and accompanying documentation, the facts concerning this matter are as follows:

On May 2, 1974, the Bank made a $95,000 loan to the Village, Ltd., which was covered by SBA's 90 percent guarantee under the

Loan Guaranty Agreement dated January 1, 1973, between SBA and the Bank. On February 6, 1975, the Bank notified SBA of the borrower's delinquency of 30 days. Subsequently this default was cured.

On May 2, 1976, the borrower again defaulted, but the Bank failed to give SBA written notice of the new default until September 3, 1976. However, the report of the loan specialist, as amended in a subsequent letter to our Office from the certifying officer, specifically states the following with respect to the Bank's notice of default to SBA:

> "Even though no written documentation is on file from date of default (5-2-76) until 9-3-76, Bank and SBA in telephone conversation knew of borrower's delinquency. Constant follow-up has been maintained by Bank at all times."

We have informally been advised by SBA that the telephone conversation in which the loan officer was first notified of the May 2 default took place on or about June 9, 1976. The report of the loan specialist also indicates that the Bank had been in constant touch with him as well as the borrower in an effort to keep the loan current. Various actions were taken for this purpose including reduction of loan payments (with SBA's approval) and meetings with SBA's management assistance division and portfolio management in an effort to counsel the borrower so as to prevent default.

The question as to SBA's authority to purchase the guaranteed portion of a loan when the lender has not complied with the notice requirements set forth in SBA's regulations as well as the Loan Guaranty Agreement was first considered in our decision B-181432, February 19, 1976. In that decision, we held that SBA could not legally purchase loans guaranteed pursuant to section 7 of the Small Business Act, as amended, 15 U.S.C. § 636(a) (1970), unless the lending institutions involved had complied with the requirement then set forth in the regulations and the general Loan Guaranty Agreement that they notify SBA within 30 days after the borrower's default. However, in recognition of the large number of loans of this type that had already been purchased by SBA, and considering SBA's longstanding practice of honoring the guarantee despite the failure of lending institutions to submit timely notice of default, we indicated that we would treat loans involving delinquent default notices as follows. Where the loans had already been purchased by SBA prior to the date of our decision (February 19, 1976), we said that we would not take exception to such payments. If the loans had already gone into default on or before February 19, 1976 we stated that we would not question payment, provided that SBA determined on a case-by-case basis that the United States had not been seriously harmed by the Bank's failure to give timely notice. Finally, with respect to any subsequent payments on defaults arising after the date

of the decision, we said that we would take exception if the notice requirements were not strictly complied with. In response to our decision, SBA amended the notice provision in its regulations and Loan Guaranty Agreement on March 8, and August 10, 1976 to increase the amount of time within which banks could notify SBA of a borrower's default.

On May 2, 1976, when Village, Ltd. defaulted on the instant loan, the applicable regulatory provision, as well as the pertinent paragraph in the Loan Agreement, read in pertinent part as follows:

> "* * * the guarantee of any loan shall be terminated if written notification of default is not received by SBA within 90 days after uncured default by the borrower. Late receipt or nonreceipt of such required notice will be excused only where written notification was sent by registered or certified mail not later than the fifth day, or by mailgram not later than the third day, prior to the ninetieth day after the original date of the uncured default. * * * the lender shall be responsible to establish and to retain evidence of delivery of the required written notification to SBA."

At this time the regulations further provided that SBA would not pay accrued interest on a loan if notice of default was not received by SBA within 45 days of the borrower's default. These provisions are controlling here.

In the present case, it is undisputed that SBA was not notified in writing of the borrower's default within the prescribed 90-day period. However, SBA was made aware of the default within the 90-day period by means of at least one and possibly several telephone conversations with Bank personnel. The sole issue to be resolved is whether, in these specific circumstances, such oral notification to SBA constituted sufficient compliance with the provision in question so as not to invalidate SBA's obligation to purchase the loan.

Although we did indicate in our 1976 decision, supra, that we would take exception to any future payments on defaults arising thereafter, "if the notice requirements are not strictly complied with," that decision addressed the issue of the timeliness of the required notice rather than any specified form of notice. Moreover, the purpose of the notice requirement is to insure that SBA receives prompt notice of the borrower's difficulties so as to be able to protect the Government's interest as well as provide timely assistance to the small business borrower. It would appear that this purpose is served once SBA has received actual notice of the default, whether oral or written, provided such notice is timely.

This is basically the position advanced by SBA's Acting Deputy General Counsel in a legal memorandum concerning SBA's liability to purchase the instant loan:

> "If, as a matter of fact, SBA was aware of the borrower's default within 90 days thereof purchase of the principle [sic] amount of the GP [guaranteed portion] would be justified, regardless of when written notice was received from the bank. Indeed, if SBA knew of the default within 45 days, SBA could also pay interest.
>
> "In giving to informal or oral notice of default the same legal effect as it would give to written notice, SBA would not be violating the principles laid down in the Comptroller General's decision of February 19, 1976.
>
> '* * * this case does not present a question of "no notice" or of "delayed notice" but solely the question of the deficiency of a notice, which was given to the proper party, was timely in full, but was not in writing.
>
> 'There are in the books a number of cases wherein casualty insurance companies have been required to pay losses where oral notices only had been given * * * [citations omitted]'
>
> "Federal Surety Company v. Guerrant, 38 S.W. 2d 425 at 428 (Ky. Ct. of Appeals, 1931).
>
> "By purchasing the GP under the circumstances, SBA is not waiving the benefit of a contractual provision but merely waiving a formality. SBA is not waiving the requirement of timely notice of default, but merely the requirement that the notice be in writing.
>
> * * * * *
>
> "The purpose of the notice requirement written into SBA's guaranteed agreement is to make sure the SBA receives notice of default in sufficient time to minimize its probable loss, and to take such steps as might be necessary to assist the Small Business borrower; that purpose is served when SBA receives timely actual notice, as seems to be the case here."

In the private commercial insurance world, it has generally been held that where an insurance policy provides that written notice to the insurer is a condition precedent to liability, oral notice is not sufficient. See Appleman, Insurance Law and Practice, §§ 3533, 4737; also see, Corbin v. Gulf Insurance Company, 125 Ga. App. 281, 187 S.E.2d 312 (1972); Orkin Exterminating Company, Inc., v. Stevens, 130 Ga. App. 363, 203 S.E.2d 587 (1973); Martinson v. American Family Mutual Insurance Company, 63 Wis.2d 14, 216 N.W.2d 34 (1974); Associated Indemnity Corporation v. Garrow Company, 39 F. Supp. 100 (S.D. N.Y. 1941). However, for the reasons set forth hereafter, it is our view that in the circumstances of the case under consideration here, this general rule should not be followed.

A significant exception to the general rule that oral notice does not suffice when written notice is required has consistently been recognized by the courts, where an insurer by its conduct has in effect waived the requirement that notice be in writing. See Appleman, supra, § 4737 and cases therein; also see Jack v. Craighead Rice Milling Co., 167 F.2d 96 (8th Cir.) cert. denied sub. nom. New Amsterdam Casualty Co. v. Craighead Rice Milling Co., 334 U.S. 829 (1948); Booth v. Seaboard Fire and Marine Insurance Company, 285 F. Supp. 920 (D. Neb., 1968); Korch v. Indemnity Ins. Company, 329 Ill. App. 96, 67 N.E.2d 298 (1946); Federal Surety Company v. Guerrant, 38 S.W.2d 425 (1931). Although these decisions do vary to some extent as to the type of insurer conduct that must be demonstrated in order to show that a waiver has taken place, relatively little proof is generally required by the courts.

In the case of Porter-Lite Corporation v. Warren Scott Contracting Company, 126 Ga. App. 436, 191 S.E.2d 95 (1972), it was held that a written acknowledgment of the oral notification by the prime contractor constituted a waiver of the requirement that the notice be in writing. In numerous other cases it has been held that mere acceptance of the oral notice by an authorized agent of the insurer without insisting on formal written notification constituted a waiver of the requirement that notice be in writing. See WeatherWax v. Royal Indemnity Company, 165 N.E. 293 (1929); Madison v. Caledonian-American Ins. Co., 43 N.E.2d 245 (1940).

While it is generally true that a Government official has no authority to waive a requirement of a statutory regulation, we believe that in the particular circumstances of this case the requirement of written notification, which is essentially procedural, was, in fact, waived by SBA and that the Bank relied on this waiver. First, it is clear by the very language of the submission made to us, as well as the loan specialist's report, that the fact of the Bank's oral notification to SBA has been acknowledged by that agency. Also, it does not appear that the SBA officer who received oral notice of the default ever suggested to the

Bank that this notice was not sufficient. It would not have been unreasonable in these circumstances for the Bank to believe, on the basis of SBA's conduct, that SBA had in effect waived the requirement that notice be in writing.

As previously stated, the general rule is that officers and agents of the Federal Government have no authority to waive or otherwise disregard statutory regulations or vested contractual rights. This was pointed out in our original decision B-181432, February 19, 1976, supra, in which we said that SBA could not waive the regulatory and contractual requirement that a bank had to notify SBA of a borrower's default within 30 days thereof as a condition precedent to the Bank's right of recovery. Also, see other cases cited in that decision.

However, these cases have generally involved substantive provisions that were highly material if not central to the relationship between the Government and the non-Governmental party. In the original "notice" decision, SBA actually made the argument that the 30-day notice requirement could be waived because it was a relatively minor and subordinate procedural condition. That view was rejected in our decision in which we said the following:

> "* * * This requirement clearly represents more than a convenience to the agency. Rather, it effects the basic and contractual relationship between SBA and the lending institutions and was obviously intended to protect the legitimate interest of the Government as well as the small business borrowers.
>
> * * * * *
>
> "Thus, contrary to the assertions in SBA's report we believe that the 30-day notice requirement is a significant and material device to protect the Government's interest. Moreover, this requirement is at least equally important, in our view, to the interests of the small business borrowers in terms of providing a mechanism to make SBA assistance available in time to do some good. * * *"

However, the issue in the present case involves the requirement that the notice adhere to a particular form rather than the more basic issue considered in the original opinion of whether notice in any form was an absolute requirement. We believe that this issue of the form of the notice can properly be categorized as procedural and that precedent does exist

to allow a waiver in such circumstances, especially where the waiver would not appear to result in any injury either to the Government or non-Government party. For example, in Sun Oil Company v. Federal Power Commission, 256 F.2d 233 (5th Cir. 1958), which involved the authority of the Federal Power Commission to modify in effect certain of its procedural rules, the Court said:

> "* * * an administrative agency is not a slave of its rules. National Labor Relations Board v. Grace Co., 8 Cir., 1950, 184 F.2d 126. Ad hoc changes may be applies retroactively. National Labor Relations Board v. National Container Corp., 2 Cir., 1954, 211 F.2d 525. In a particular case an administrative agency may relax or modify its procedural rules and its action in so doing will not be subjected to judicial interference in the absence of a showing of injury or substantial prejudice. National Labor Relations Board v. Monsanto-Chemical Co., 8 Cir., 1953, 205 F.2d 763."

Also see American Farm Lines v. Black Ball Freight Service, 397 U.S. 532 (1970) and cases cited therein.

In addition to the foregoing, we believe that the same result is justified upon consideration of the intended purpose of the requirement that notification of default be in writing. This was discussed at some length in the case of Iowa Mut. Ins. Company v. Meckna, 180 Neb. 516, 144 N.W.2d 73 (1966), as follows:

> "Having determined that Meckna is an additional insured, we now consider insurer's contention that Meckna breached the notice and cooperation provisions of the policy. Considering first the notice provisions we quote: 'In the event of an accident, occurrence or loss, written notice containing particulars sufficient to identify the insured and also reasonably obtainable information with respect to the time, place and circumstances thereof, and the names addresses of the injured and of available witnesses, shall be given by or for the insured to the company or any of its authorized agents as soon as practicable.' What is the purpose of this provision? Patently it is to alert the insurer to a possible claim and to afford it an opportunity to make such investigation as it deems pertinent to enable it to process any future claim. Here, the insurer had actual notice of the collision involving the automobile covered by the policy, and of the death of the named insured within hours of the tragedy. Actually, the agent who sold the policy called insurer the morning after the collision.

> Its resident vice president visited with Meckna within less than 24 hours thereafter, and within a few days thereafter it had procured a copy of the police report. Its own file discloses that within 4 or 5 days thereafter, it knew that Meckna was the driver of the car, and that she had corrected her first report to the police. * * * The record would indicate that insurer also knew of the availability of other witnesses soon after the accident, and while the record does not indicate that they were interviewed by insurer, the original police report listed the driver as unknown because these witnesses had given the information that a women and not the deceased was driving the automobile. Insurer had all the information Meckna could give it, and had ample notice to permit it to take any and all necessary steps to protect its interest. Under the facts in this case, there is no merit to this assignment." (Emphasis added.)

As this case suggests, the general rule in the commercial insurance field that a requirement of written notice is not satisfied by oral notice is based on the insurer's need for very specific information and full particulars in order to allow it to conduct a complete investigation and thereby fully protect its own interest. As stated in that opinion, if this need is satisfied by some means other than that strictly called for in the contract of insurance, the insurer should not be allowed to avoid its obligation on that basis.

Similarly in the case at hand, where all that is required is a simple notice of default without other particulars, we believe that the oral notification that was given was sufficient to provide SBA with all of the information that was necessary to protect both the Government's interest as well as the interest of the small business borrower.

In accordance with the foregoing it is our view that in the specific circumstances of this case, SBA need not treat the guaranty as terminated by the Bank's failure to give SBA written notice of default within the prescribed 90-day period, and we do not object to the certifying officers certification of the claim in the amount of $69,080.82 representing the guaranteed percentage of the loan principal.

With respect to the question of whether SBA should pay accrued interest on the guaranteed percentage of the principal amount, we note, as stated above, that the regulations in effect when the default occurred provided that SBA would not pay any interest on a loan if notice of default was not received by SBA within 45 days thereof. Based on the information informally provided to us by SBA that the oral notification was

actually received by SBA on or about June 9, 1976, which is well within 45 days of May 2, 1976, it would appear that SBA would be authorized to pay the accrued interest.

R. F. Keller

Deputy Comptroller General
of the United States